Professional Indemnity Initiative
5.2 updated

A Guide to Professional Indemnity Risk Management for General Insurance Broker Staff
For the purpose of this guide the following definitions are used:

**Client:** A proposer for insurance; a policyholder who is the client of an insurance broker; whether or not the broker interacts with the client face to face, or remotely, or a combination of both or perhaps with another insurance broker.

**Broker:** Means insurance broker or intermediary.

**Insurer:** Means the insurance company or syndicate or company at Lloyd’s.

**Onerous terms:** Means unusual, or significant, or onerous terms, conditions and limitations in a policy or attached thereto by endorsement or addendum. These can include, but are not limited to, pre-conditions to liability under the policy, conditions precedent, warranties, exclusions, complex excesses and the like.
Modern Broking & E&O
A Desk-Top Guide for the professional insurance broker

Good practice; Improved reputation; Increased profitability
A general insurance broker / intermediary will almost certainly, at some time, attract criticism that could develop into an Errors and Omissions (E&O) / Professional Indemnity (PI) claim.

The reasons for this stem from the fact that:-
a) Mistakes can be made in even the best run business and
b) Client’s expectations of insurance are often greater than we realise.

There are three good management reasons for a broker to take care to avoid E&O / PI claims:
1. They are time consuming, stressful, expensive to deal with and damaging to your client relationship and your reputation.
2. They imply fault with the broker’s FCA regulatory compliance standards.
3. They cost the business money: the policy excess, unrecoverable costs and time in defending the claim and increased PI insurance premium following the payment of a claim – all of which hit the bottom line.

All of the above affect reputation and profitability
This PI guide will help you to be aware of the risks and opportunities that can derive from modern insurance brokering.
TEN TOP TIPS

1. Know and understand your professional duties and legal responsibilities as an insurance broker, with particular reference to FCA regulations; the laws of agency and the common law duty of care and any code of conduct that you are bound by.

2. Be aware of what can cause a complaint or claim and what constitutes a “circumstance that could give rise to a claim”.

3. Know and understand the relevance of demands and needs statements as defined in ICOBS 5.2.2 and how they can potentially create a liability, particularly if you have not actually assessed the client’s insurance demands and needs.

4. Know how to recognise a potential PI claim/circumstance in the making and what to do next.

5. Know when (and how) to ask for guidance or advice from peers or line managers.

6. Know how to create a complete and accurate written record of your advice, recommendations and communications. This may provide valuable defensive evidence and will assist your clients and colleagues if you are not available.

7. Beware of the traps that lead to underinsurance, especially in valuations of property and in business interruption insurance calculations and the basis of settlement generally.

8. Never rely upon your client to know what an Insurer would consider to be material information. You must advise the client on the duty to disclose material information to insurers (and the sort of matters which should be disclosed) and explain the consequences of failing to disclose material information and breaching the duty of disclosure.

9. Never write something in an email (or anywhere else) that you would not want read out in public, to your employer, or in court. Preferably, send terms and advice in a letter or quotation template (attached to an email if appropriate), ideally checked by a peer before it is sent. If you want the court to judge you as a professional person you must act like one when corresponding with others and keeping notes.

10. If you do not actually know something for certain, say so; do not guess and do not make it up to get a sale or seem impressive.

Remember - Treating Customers Fairly requires:

- Fair treatment
- Products designed to meet the needs of identified consumer groups
- Clear information before, during and after point of sale
- Suitable advice which takes account of their circumstances
- Service of acceptable standard
- No post-sale barriers to change product, switch provider, submit a claim or make a complaint.
The template for managing PI risks, this is not an exhaustive list but will help to assist in identifying issues including:

**Law and regulations**
2. Breach of contract (TOBA).
5. Inadvertent mis-selling; reckless mis-selling; deliberate mis-selling.
6. Mis-description or misleading-promotion of insurance products/services.
7. Failure to comply with ICOBS/TCF regulations.
8. Failure to recognise or disclose conflicts of interest.
9. Failure to comply with codes of conduct.

**Instructions and operational**
1. Failure to effect insurance cover that meets the client’s demands & needs (lack of suitability).
2. Failure, when transferring cover to a new Insurer, to ensure the new cover provides at least the protection which the client previously enjoyed (continuity) or that the client is warned of any differences.
3. Failure to place or renew an insurance policy.
4. Failure to execute a client’s instructions.
5. Failure to record client’s instructions.

**Advice**
1. Failure to properly advise, particularly in relation to:
   a. Obligations of disclosure of material information. (see p.13)
   b. Limit of indemnity/sums insured/basis of settlement.
   c. The risks of underinsurance; the application and meaning of the Condition of Average.
   d. Business interruption –
      (i) the difference between an accountant’s understanding of terms, such as turnover and profit and the insurance meaning of these expressions.
      (ii) How the client should assess and calculate business interruption sums insured.
      (iii) How the client should choose an appropriate period of indemnity for business interruption.
2. Conveying the meaning and implication/s of warranties or special terms and conditions to the client.
3. Reasonably ensuring that the client has understood the advice and warnings brought to their attention.
4. Failure to advise client of the consequences of non-compliance with warranties, terms and conditions.
5. Failure to recognise and deal with ambiguities in policy terms and conditions.

**Dealing with a Client**
1. Not correcting errors in terms and conditions quoted prior to inception of contract.
2. Causing or not preventing unreasonable delay in provision of terms and quotations.
3. Failure to bring matters to the attention of the designated line manager or compliance officer of the client organisation.
4. Failure to ask the client the right questions to elicit material facts.
5. Failure to advise where clients’ contracts, promises or undertakings can conflict with and/or potentially negate insurance cover.
6. Failure to advise client of options and choices in selection of insurance terms and conditions.
Claim notification and advising on claims matters
1. The policy obligations of claims notification.
2. Failure to notify claims or circumstances on behalf of the client. (including excess layers).
3. Failure to advise, proactively about the management and negotiation of claims.

Dealing with insurers
4. Failure to communicate information between client and insurer – both ways.
5. Failure to present fairly the information as provided by the proposer client.
6. Failure to communicate material information to Insurers on behalf of the client.
7. Documentation / endorsement drafting errors.
8. Failure to check that issued policy documents meet client’s demands and needs.
9. Failure to document fully the presentation of the risk.

Case Study

This case study brings to life some of the failures mentioned above. A broker was instructed by its client to reduce the sum insured on the buildings and contents policy and also on the business interruption policy. The broker advised the client, in writing, on three occasions, that it was “not advisable to reduce the sums insured” because, by the calculations and experience of the broker, the business would be under-insured.

The client insisted, telling the Broker that their accountant had advised that they were over-insured and that significant premium could be saved.

The broker carried out the instruction, “because it was in writing”, but knowing that it was most likely that substantial under-insurance existed.

A claim occurred in the same policy period and insurers denied liability on several grounds including:
- Misrepresentation of material information by the broker – who knew/believed the client was underinsured and did not tell the insurer.
- Misrepresentation of material facts concerning the nature and profitability of the business - the accountant’s figures were later proved (by loss adjusters) to be factually wrong.

The claim against the broker succeeded and was settled out of court for an undisclosed sum equaling the full limit of indemnity of the Broker’s E&O policy.

An insurance broker should recognise the legal implications of accepting instructions from a customer to do something that the broker knows or believes to be any part of the following:
- wrongful in good and reasonable insurance practice,
- deceitful of an insurer or otherwise against the best interests of the insured
- or that it has advised against.
What is the root cause of most E&O/PI Claims?

More than 75% of E&O/PI claims are the result of a failure in communication

Failures of communication are often by omission. Failures can be in the written or spoken form and may result from unspoken implications or assumptions. The failure in communication may not originate from the broker; it may originate from the insurer or from any other party involved in the insurance process, but the broker could be held primarily responsible because a client is entitled to rely upon the advice and services of the broker.

Management responsibility to set the parameters

It is the responsibility of management to set the standards and processes for communicating with clients in a way best suited to the nature and volume of its business so that it will meet the standard of care to be expected of a reasonably competent broker, such that all personnel can reasonably be expected to conduct the business in accordance with those required standards.

Some useful tips to guide the broker include:

Oral communication

Much of what a broker will do in the course of business is by way of spoken word; oral communication. Clients will often hear and take in only part of what is said. Brokers will not know what part has not been heard. It is therefore essential, for good record management, that brokers keep a written record of the key parts of conversations and in particular any instructions given or received. It is good practice to adopt a procedure and format for noting conversations with clients and insurers so that the file contains a written record (including date and time) that can be easily followed by whomever goes to the file in a broker’s absence. These records will be of significant benefit to the broker in the event of a complaint or dispute. Any record should be identifiable to the person/s involved and signed and dated by the person making the note. An electronic data tag is sufficient.

Emails

The convenience of emails and the unsupervised privacy in which they are written has given rise to an unprecedented commercial risk. Use of shorthand language in email and text is entirely inappropriate for business correspondence with a client. Shorthand is acceptable between peer practitioners as long as ANY peer practitioner can pick up the file and understand what has been recorded without any reference to a third party. Rather, all business correspondence with clients is better conducted in a formal style (or in a standard template) using clear and jargon-free language that conveys the intention and meaning with clarity and certainty. Where insurers use expressions in insurance jargon do not change them but, rather, explain them to the client.
**Reports, quotations, recommendations and advice**
Any of these communications and others that have a similar level of importance, are more likely to be sound in content and purpose if they are written in a formal style and on the company’s letter head or in specially designed quotation or report templates to suit the broker’s business style and operational processes. Such documents can then be attached to emails for speed and convenience of delivery.

**A peer review**
process can also be used before reports and other key communications are published to a Client, to ensure they include all the information intended and required to be conveyed for complete and accurate advice and to detect errors, omissions, misrepresentations or misleading information.

**Conclusions and recommendations**
these should be set out separately within the communication giving reasons for them when an explanation is called for to ensure they are properly understood.

**Advice and warnings**
included in the communication should be separately and clearly labeled as such.

**Onerous terms**
should be clearly labelled so that the can be easily referenced by the reader in the full policy document. The consequences of failing to adhere to any obligations imposed by such terms and conditions should be clearly spelt out. More is said about this below.

**Record keeping – an essential practice**
In the event of a complaint or claim the records kept by the broker will be minutely scrutinised by lawyers and investigators seeking to find fault and to attach blame. Absence of clear and continuous records can leave the broker seriously exposed to potential liability in law; without written records to rely on a court may well favour the evidence of the lay client over the professional adviser (broker).

The task of collating records from different media, including email, web sites, policy and financial related documents, schedules, forms, file notes and other typical broking materials and then creating a complete audit trail is, admittedly, burdensome. Consequently, it often fails to be done. It is the responsibility of management to organise the keeping of records so as to encourage good record keeping as an ordinary part of everyone’s job and do so in a way that is suitably time and cost efficient. The prospects of a successful defence of a claim may be undermined where contemporaneous and other appropriate evidence is absent.
As soon as there is any suggestion of a PI claim, the court rules require you to preserve all disclosable documents. This includes electronic documents, such as emails, excel or word files. At this stage it is extremely important that no electronic documents, which might be connected with the case, are altered or destroyed (even if they would normally be in the ordinary course of business).

Wilful or reckless destruction or changing of evidence can lead to criminal prosecution.

**Good communication skills**

Insurance is complex and highly technical and based on a legally binding contract and associated duties of utmost good faith. Policies of insurance still tend to use jargon, phrases, expressions and special meanings unique to the industry and with which clients will be unfamiliar. It is the broker’s duty, without exception, to use reasonable care and skill in conveying the terms of the insurance to the client in a way that they can reasonably be expected to understand and also to bring to their attention any unusual onerous or significant terms and conditions.

Lastly, it is important to convey, openly and clearly, to the client, the **consequences** of failing to comply with such terms and conditions.

Ineffective communication can cause the broker to be held to blame for things that go wrong and cause loss or damage to the client. Time and commitment to precise, complete and intelligible communication is a prime responsibility of the broker.

It is the responsibility of every member of a broking business to take care in what they do and to report things that might lead to a breakdown in communication or a complaint or claim, to their line manager.

NB. There is also a regulatory duty to record complaints and report them on a regular basis to the regulator.
Good practices for the broking process

It remains the responsibility of management to adopt and maintain a system of work and procedures that will ensure that the broker’s obligations to its client are reasonably met and that they will meet the broker’s obligations for the management of risk. These may vary according to the nature of the insurances sold and the method of selling.

The legal obligations of an insurance broker are not diminished (in law) by reason of the cost to the broker of meeting them.

Demands and Needs of your client
An insurance broker should only arrange a policy that meets the demands and needs of the client. It is therefore essential that you know what are the demands and needs of your client. You can only do this by asking questions and finding out, so that you are satisfied that the policy will meet the client’s demands and needs.

An insurance broker is presumed to know more than their client about insurance and what a client will need. A client is entitled to rely upon a broker for having the knowledge and skill ordinarily to be expected of a reasonably competent broker.

In many cases today the insurance broker will not actually meet the client and never converse with the client face to face. Nevertheless, the duty owed in law to that client is not diminished by such fact.

Record the critical facts of the client’s instructions.
If dealing with a client face to face, or by telephone, record in your file/attendance note and refer to in your written confirmation to a client:-
- Specific information imparted by the client,
- The timescale for action,
- Whether time is of the essence,
- Any reliance you have placed upon something that the client (or someone they rely upon) must do as a result of the instructions.
- Any other conditions, impediments to action or restrictions that may prevent the instructions being carried out. If your instructions are received remotely by automated process, then it is the responsibility of management to adopt a process that records instructions to a similar standard.
- Sign and date all records either by hand or electronically.

Acknowledging instructions
All instructions from clients, whether in writing, by telephone or at a meeting, should be acknowledged in writing, or some other permanent and recordable form. The purpose is to give the client an opportunity to see that the broker has understood the instructions and to tell the broker if they are not correct. If this is done
by automated templates the process should be capable of achieving that objective.

This requires a concise communication to the client stating exactly what you have understood their instructions to be and confirming what the broker intends to do as a consequence. Say also that, if this is not in accordance with their intended instructions, they must advise the broker without delay, otherwise it intends to proceed on the basis that the instructions are correct.

**Client’s understanding and receipt of communications**

It is a broker’s responsibility to use reasonable skill and care to satisfy itself that its communications have been received by the client. If the broker is in any doubt as to whether its client has received its communication, it is prudent to check. Do this within a few working days of sending it, or sooner, if there is urgency. If there is no response send a reminder. Do not just assume it has been received or that clients have read it.

It is also a broker’s duty to take reasonable steps to satisfy itself that where there are onerous terms in the insurance that the client understands the nature and implications of such. E.g. a warranty that a deep fat fryer must have an automatic cut-out switch. If an insurance broker believes that a client understands an explanation that has been given (normally in a person to person situation) there is no reason why the insurance broker should not note and date this on file. Remember it is the opinion of a professional person that is being recorded and if well made there is no reason why a judge should dismiss this assessment perhaps even years later.

**Preparing to place the cover**

Cover may be offered/given subject to pre-conditions, warranties, exclusions or other specific obligations.

**For example:-**

- Theft precautions
- Survey requirements
- Alarm and other warranties
- Improvements in security, management of processes or procedures
- Confirmation of something to be done or not done, installed or removed
- Time limits given for compliance with specific requirements

**Be aware that your client may be:-**

- Unwilling to comply
- Unable to comply for reasons of lack of authority in the business
- Unable to comply for financial reasons
- Apathetic and reckless as to whether they comply or not
- Relying upon the belief they can always sue the broker if there is a coverage problem
- Unaware of the need to tell insurers of incidents that were not claims under the policy, but which nevertheless cause loss or damage and that could affect a prudent underwriter’s assessment of the risk.
It is the broker’s responsibility to act appropriately if any of the above are known or suspected. Appropriate action is to refer the matter to your line manager.

**Communicating onerous terms**

A competent broker is expected to know if terms and conditions are onerous terms. If in doubt seek help from your line manager.

Communicating onerous terms is particularly important. Brokers’ failure to communicate these effectively has led to them being successfully sued for negligence. In today’s highly automated business environment it can sometimes be operationally difficult to convey information that falls outside what is normally sent to a typical client. Nevertheless it is a sensible practice.

In each case the meaning, implications and obligations imposed upon the client should be spelt out, explaining:

1. The scope and limitations of cover actually given, and
2. The consequences of non-compliance; so that there can be no reasonable doubt at a later date that a complete, fair and unambiguous explanation has been given to the client.

**Significant Information**

Bringing significant information, such as onerous terms or other matters peculiar to your client, to the attention of your client requires special means. This is where, for example, a formal letter on company notepaper can carry more weight than the same message being communicated in the body of an ordinary email. The broker may also consider the additional value of sending the letter by post, if in the circumstances the broker believes it may attract the attention of the client more easily.

**Distance Marketing – Communicating onerous terms**

It is recognised by the FCA that in distance marketing not all the necessary or recommended information can be provided to the client before inception and/or renewal of the contract. ICOBS 3.1.15R says:-

“A firm may provide the distance marketing information and the contractual terms and conditions in writing or another durable medium immediately after the conclusion of a distant contract if the contract has been concluded at a customer request using distant communication that does not enable the provision of that information in that form in good time before conclusion of any distant contract”

**What to include in the communication**

The purpose of the communication is to convey something important or significant. It should therefore be straightforward and clear; not wrapped up in insurance jargon or language that can confuse or obscure the point the broker is intending to make.

The prudent broker will take reasonable steps to satisfy itself where possible that the client understands both the nature and effect of such the onerous terms and related advice and the consequences of not complying with them.
The broker could try to encourage the client by any reasonable means:

1. to read the onerous terms and any related advice;
2. to confirm if possible, to the satisfaction of the broker, that they have understood any onerous terms and any related advice; or
3. to tell the broker that they have not understood all or part of it.

Caution:

It is not good practice to tuck this kind of information or warning away in the body of renewal letters, quotations, proposals or any other compliance or template documentation. The broker may be judged to have failed in its duty to its client if it does so. (See “What the Courts Have Said”, below)

It is not good practice, either, to rely upon a client signing a duplicate copy of a broker’s letter. A court may not regard that as effective communication.

It is not good practice to use standard template warnings that are likely to be missed or ignored by the recipient. Make them noticeable even if it means using non-traditional vocabulary, different colours, boxes, warning signs!

Disclosure of material information

It is necessary for an insurance broker to remind the client at inception of the first insurance and at each renewal thereafter, of the proposer’s duty of disclosure of material information and the effect of non disclosure.

A material fact has been discussed in various legal cases. Broadly it is any fact which may influence the judgment of a prudent underwriter in deciding whether to accept a risk and if so at what terms.

This should be communicated in a clear and easily noticeable manner and, as with the warnings mentioned above, it is not good practice to tuck this kind of information or warning away in the body of client letters, quotations, invoices or on the back of documents or any other compliance or template documentation. A broker may be judged to have failed in its duty to its client, if it does so.

The client might also be reminded about the need to verify other significant information such as the value/s of the property or subject matter at risk (the sum insured) and be sure not to understate those values.
Consumer Insurance (Disclosure and Representation) Act 2012

The Consumer Insurance (Disclosure and Representations) Act (“the Act”) gained Royal Assent in March 2012, and came into effect in April 2013.

It has given consumers (but not the business policyholder) some relief from the onerous demands for pre-contract disclosure of material facts that exist in insurance law under the heading of utmost good faith. It DOES NOT relieve the consumer of telling the truth or being honest and fair in the information given in accordance with the ordinary rules of material disclosure.

The Act is concerned only with “consumer, personal insurances wholly or mainly for purposes unrelated to their trade, business or profession”. This would include, for example, cars with occasional business use. The new Act’s purpose is to improve the balance between insurers and policyholders with regard to disclosure of material information and clarify the practical effects and implications of “misrepresentation”.

Mixed use of contract

If you are concerned whether that an insurance may be a combination of consumer and business insurance then you should recommend full disclosure of all material facts as though the terms of the Act do not apply. Always seek advice if you are unsure.

A Consumer proposer’s duty

Under section 2 of the Act, it is the duty of the consumer proposer to take reasonable care not to make a misrepresentation to the insurer before the contract is entered into, or varied (“the duty”). This modifies the current consumer’s duty of ‘utmost good faith’, by removing the obligation to disclose all material facts. The consumer proposer will no longer be required to volunteer information but only need respond as required under the duty.

Not responding to an insurer who asks for confirmation of material facts may amount to a misrepresentation.

The Act sets out what is meant by taking reasonable care. The test is an objective one, namely, the care a reasonable consumer should take. If there is a dispute all the circumstances leading to the misrepresentation will be considered, including the nature of the insurance, its target market, the information about the insurance published by the insurer, the precision of the insurer’s questions and how important the insurer indicated they would be. If an agent, e.g. a broker is representing the consumer this will be considered as well. Dishonest misrepresentations will always be taken as showing a lack of reasonable care.

To further clarify the remedies, a qualifying misrepresentation is either deliberate or reckless or careless. A deliberate and reckless misrepresentation is one when the consumer knew or did not care that it was untrue or misleading. Any other misrepresentation will be careless.

The Act considers the position of agents in consumer contracts and sets out a test and examples of how to determine when an agent is that of the insurer or the consumer. A broker or an intermediary will be an agent of the consumer when asked to obtain an
insurance contract for the consumer. A broker may also be an agent of an insurer at the same time, e.g. when it is operating as an underwriting agency or under a binding authority of any kind of the insurer. A full copy of the Act is available at www.legislation.gov.uk/ukpga/2012/6/contents/enacted

Continuing duty of material Disclosure

It is important to establish whether the policy arranged for the client contains a condition that requires material information to be disclosed during the period of the policy. If so it should be regarded as an onerous term and dealt with and explained to the client accordingly. Remember that the duty of continued disclosure during the term of the policy is contractual rather than legal so make sure you study the actual wording in the policy.

In summary – Primary Issues

A broker is at risk if it has not taken all reasonable steps to ensure that:

1. The client’s demands and needs for insurance have been met. (i.e. the policy is suitable for the client)
2. You record critical facts and instructions, accurately. (Perhaps to the standard that a peer practitioner could understand the case from your file without referring to anyone else)
3. Acknowledge instructions - to check for misunderstandings.
4. You communicate onerous terms effectively to the standard that the client can make an informed decision.
5. You do not tuck important information away in the documentation pack, instead, direct the customer to where they can find it.
6. The client understands their obligations about disclosing material information.
7. The client understands the importance of complying with onerous terms and the potential consequences of non-compliance; e.g. breach of
warranty may lead to the policy being void from the start.
8. Your communications have been fair reasonable and are easily understandable by the client.
9. If you genuinely think the client has understood what you have explained then make a file note and date it.
10. Remember the Four key rules
(i). Gather sufficient information to make a fair presentation of the risk and to recommend insurance arrangements which are suitable for the client’s Demands and Needs.
(ii). Give sufficient information that the client can make an informed decision about the recommendations you make.
(iii). Keep records to the extent that a peer practitioner can pick up your file and run with the case without any reference to anyone else if something were to happen to you.
(iv). Make a note of what you explained to the client and whether you thought they understood.

What can an insurance broker do to prevent E&O/PI claims?

We cannot prevent someone making a claim against us, but we can avoid giving them a reason to do so.

This requires :-
1. An appreciation of the role and legal duties and obligations of a broker.
2. Systems of work and procedures that are designed to protect the broker from inadvertent errors and omissions in the course of daily work.
3. An awareness of the risks associated with being a member of a professional, whose practitioners advice is relied upon by the client.

Professionalism – know how you are seen and judged by others.
A modern broker is a professional adviser and a member of a profession. The standards by which a broker will be judged are those expected of a professionally skilled adviser owing a professional duty of care. The law does not recognise a broker as being only a seller of goods or services, without responsibility unless there is a specific contract between the insurance broker and client to that effect.

The modern law concerning insurance brokers is governed by:-
- LAW of Agency
- Common Law Duty of Care
- Laws of Contract
- Statute Law
- FCA Regulations
- Codes of Conduct and or Codes of Ethics

Primary role and duty
The primary role of the broker is to act as agent of the client, to act as professional adviser in respect of insurance matters and to provide services to those seeking the benefit of insurance. The role is wide and
includes not only arranging the policy, but also the giving of advice on the policy/ies (except for non-advised sales) and in making claims under the policy/ies.

A duty of care is owed by the broker to the client. The broker must also be aware that it may assume a duty of care, sometimes without appreciating it, to persons who may not be its client but who may nevertheless rely upon the broker’s advice and services.

In addition obligations are owed to the client in contract according to the Terms of Business Agreement (TOBA). FCA Regulations also create obligations to a client. A broker should know and understand how these interact with their common law duty of care.

Ultimately, it is for the court to decide what a reasonably competent broker should do or not do, according to its duty of care and/or its contractual obligations. The view most recently expressed by the courts is that brokers should achieve such standard which, in the opinion of the court, members of a “profession” (of brokers) ought to achieve. While the precise conduct expected of a broker will vary from case to case, according to circumstances, the court will expect a basic threshold of reasonable competence and good practice from the broking profession. The standards of care will be assessed as those expected at the time of the alleged negligence.

An insurance broker cannot rely upon the simple defence of: “I carried out the instructions of my client”. Simply reacting to a client’s instructions may not be accepted by a court.

A member of a profession such as insurance broking is required to give its clients proactive advice using its own judgment (and where necessary, warnings) about their insurance arrangements and, specifically, their demands & needs. (See below)

Conflicts of interest
The broker may also have separate legal obligations to insurers and underwriting agents, concurrently with its obligations to its client. Conflicts of interest that must be recognised, recorded and properly managed.

Conflicts of interest are an ever-present danger to the modern broker. They are always closely examined in E&O claim situations. A broker who has any authority from an insurer, to accept and bind business, is in a potentially conflicting relationship with its client. Conflicts of interest can be managed, but they can be very difficult to deal with in the event of a complaint or claim because the complainant will allege that the broker has put the interests of the insurer before the interests of the client and the broker will be required to prove otherwise. Sometimes that proves to be difficult, in the extreme.

This occurs where the broker acts as the insurer’s agent; for example, in relation to a cover-holder or binding authority. This can lead to claims by the insurer against the broker, for example for issuing a policy in breach of the terms of a binding authority.

Demands and Needs
The FCA regulations concerning demands and needs are known to brokers but the implications of the regulations, in particular ICOBS 5.2.2R, are less well appreciated.
The essence of the demands and needs regulation is to reinforce the common law duty of care of a broker to know its client and to ensure that the client’s insurance needs are properly met.

It is well known by brokers that they must issue a demands and needs statement, but less well appreciated that they need to have first assessed those demands and needs; otherwise how can they issue a statement that a policy meets them? To discharge that need is easier with a large client, where there is personal interface between client and broker, but more difficult for the clients that the broker never sees or communicates with other than electronically. Nevertheless, the duty of the broker to comply with its legal and regulatory obligations is not diminished by this difference, nor by the amount of the commission or fees the broker receives. It is the responsibility of management to adopt a system of work and procedures that complies with the regulations, modulated according to the complexity of the policy being proposed.

**Regulation – A practical application of a Principle.**
A Demands and Needs Statement is intended to confirm the broker has understood the client’s insurance needs, and any more specific demands for cover and confirms a meeting of minds and that the policy proposed meets those demands and needs.

**ICOBS 5.2.2R**
1. Prior to the conclusion of a contract, a broker must specify, in particular on the basis of information provided by the client, the demands and the needs of that client as well as the underlying reasons for any advice given to the client on that policy.
2. The details must be modulated according to the complexity of the policy proposed.

At the time of writing ICOBS 5.2.2 prevails. In the event that the ICOBS are overtaken by FCA the principles of the ICOBS will probably remain the same.

It is precisely because ICOBS 5.2.2 refers to a broad principle that insurance practitioners have to understand the breadth and depth of the implications it carries, beyond FCA regulation itself. It has significant implications for the broker’s common law duty of care and for the broker’s Terms of Business Agreements (TOBAs).

It is important that brokers’ senior management fully understand the implications of the complexities arising from the co-existing inter-relationship of FCA regulation, TOBAs and the common law duties relating to modern day insurance broking / intermediation.

It is equally important to understand that the gathering of information from clients has to be accurate and effective to enable the broker to assess the demands and needs (requirements) in the context of the
products available and, thereafter, either:

(a) produce a bespoke Demands and Needs Statement (which may follow an established structure or format); or

(b) use a generic Demands and Needs Statement. (See below)

The broker must assess, in each case, whether that statement is relevant to the client. This requires an understanding of the practical effects and implications of the law and obligations and how to tackle them in practice.

**Generic Demands and Needs Statements**

Care should be taken in particular with generic Demands and Needs Statements typically adopted for high volume, low value business. It is management’s responsibility to assess the generic needs of any given class of client and take into account the exceptions that may arise and adopt a system of work and procedures that suitably meet the regulations’ requirement to be able to give “the underlying reasons for any advice given to the customer on that policy”.

**Unachievable Demands and Needs**

An inability to place insurance on terms required by the client does not entitle a broker to just place a policy on any terms, without any reference to the client. Clients’ needs and expectations are sometimes beyond what can reasonably be achieved. Brokers are often reluctant to admit this for fear of losing a client. It is a dangerous practice.

The broker’s role is to ensure that the insurance obtained properly meets the client’s demands and needs and this necessitates the broker to actively consider what particular insuring clauses, when moderated by the exclusions and conditions, will meet those demands and needs.

A broker faced with this situation should discuss with the client any inability of the policy to exactly meet the client’s stated demands and needs. They should explain the consequences of not being able to obtain the insurance to meet them.

In the event of not being in direct communication with a client the broker must have a system of work and procedures that meets the standards described above.

**Wider cover?**

Equally a broker must ensure that if cover is available that is wider or more beneficial than what is asked for, then this is also made known to the client, together with the consequences of being without it.
What the Courts have said – about a broker’s duty of care

The case of Nicholas G Jones (claimant) v (1) Environcom Ltd (2) Environcom England Ltd (defendants) & Ms plc (t/a Miles Smith Insurance Brokers) (third party) (2010) QB:) (comm) (David Steel j) 15/4/2010 demonstrated the importance of ensuring that your client understands its duty of disclosure and the potential difficulty of achieving this by reference to standard warning notes in brokers’ placement or renewal documentation alone.

Café De Lecq Ltd v R A Rossborough (Insurance Brokers) Ltd [2012]JRC 053
This case, heard in the Jersey Royal Court, concerned a broker who arranged an insurance for a beachside café without taking sufficient care. The broker used its automated quotation system and the system let the broker down. It was not capable of meeting the standards of care required of a broker:

The Royal Court commented on the broker’s automated quotation and selling process as follows:
“...(the process for selling “package” policies) is driven by considerations of speed and economy… which may have advantages for all concerned.. but it can also entail significant risks of a quotation failing to meet the insured’s needs or to reflect the true basis of cover.”

The implications of Environcom for general insurance brokers/intermediaries can be summed up as spoken by the judge, David Steel J:
“In short, a broker:
– must advise his client of the duty to disclose all material circumstances;
– must explain the consequences of failing to do so;
– must indicate the sort of matters which ought to be disclosed as being material (or at least arguably material);
– must take reasonable care to elicit matters which ought to be disclosed but which the client might not think it necessary to mention.

All this flows from the requirement that the broker should take reasonable steps to ensure that the proposed policy is suitable for the client’s needs.”
“the process is designed to minimise the time and effort that the broker has to spend on the matter and to transfer responsibility for getting things right to the client, thereby draining the broker’s role of much of its raison d’être.”

The judge went on to say:
“(the automated process) is liable to foster a situation in which the broker becomes more closely allied with the insurer whose policy documentation he is generating than is healthy, to the detriment of the client whose interest he is supposed to be looking after.

On the matter of a broker’s relationship with the client the judge said:
“It is important to remember that what we are concerned with here is not the fairness or efficacy of the contract between insured and insurer but the relationship between broker and client: a relationship of agency, the sole purpose of which is actively to help the client secure a contract of insurance on terms that will serve his needs. That this cannot be done without the cooperation of the client is of course, true; but the whole premise of the relationship is that it should accomplish something over and above what the client could do for himself were he to approach the insurer direct.”

The judge also observed that in Environcom, Steel J had said:
“(I am not persuaded that it is sufficient to rely upon written standard form explanations and warnings annexed to proposals or policy documents. I understood the experts to be agreed on this. The broker must satisfy himself that the position is in fact understood by his client and this will usually require a specific oral or written exchange on the topic, both at the time of the original placement and at renewal.)

… and [the judge said] that an observation to similar effect can be found in Youell v Bland Welch 1990.

These recent cases indicate the standards by which the courts are judging brokers.
7 Top Tips

1. **Know whether you are making an advised or non advised sale and what is meant by ‘advice’, in this context?** Refer to your compliance officer/adviser for detailed advice of what constitutes advised sales and non-advised sales in your business. It is a complicated matter and must be properly understood.

2. **Remember that a broker may be judged as a professional adviser by:**
   a) the quality and completeness of its advice and
   b) the broker’s ability to prove that its advice was consistent with the standards expected in law, of a reasonably competent broker.

3. **Assessing the client’s Demands and Needs is the first duty of a broker.** The client is relying upon the broker’s knowledge, skill and expertise to obtain suitable cover and the broker will be making a statement that says that it has assessed their Demands and Needs. If the broker has not made an assessment it cannot reasonably make that statement!

4. **Try not to confuse the client with insurance jargon and “market speak”.** Take the time and trouble to use clear and simple language to convey your message.

5. **Do not be tempted to hide behind “exclusion clauses” in TOBAs of things that are not going to done by the broker, for the client.** Tell them up front what they can expect from your service and what they cannot expect. If the broker wants to make an additional charge for additional services; say so in the TOBA.

6. **The broker needs to have suitable systems and procedures to actively and specifically explain to the client their obligations and duties relating to insurance including in particular disclosure of material facts and the potential effects of not complying.**

7. **Above all: Always record actions, advice and opinions in such a complete manner that the broker’s audit trail will provide a sound and complete record if ever it is needed in evidence or a peer practitioner needs to stand in for you and Be aware:** The legal duty of care of the modern broker is not necessarily discharged by standardised warnings and Demands and Needs Statements or by adhering to the firms compliance requirements alone. The client must be put in a position that they can make an informed decision.
The “Claims Made” E&O Policy – and claims notification

PI insurance policies are always (in the UK) written on a “Claims Made” basis. This means that the policy only covers claims made (or circumstances notified) under the policy during the period of the policy, irrespective of when the act, error or omission alleged to have given rise to the claim was actually committed or occasioned. In other words it is the policy in force when the claim is first made by the claimant (or circumstance first notified by the insured to the insurer) which will cover the claim/circumstance under the policy.

Claims Notification Conditions
These vary from insurer to insurer. While they all are intended to have a similar effect the wording of each of them differs and it is in the client’s (and the broker’s) best interest to have read and fully understood what these require of the client.

Some claims conditions are Conditions Precedent to liability. For example it may be a Condition Precedent to liability that the client will notify a circumstance or claim within seven days of discovery. If it is notified on the 8th day it is a breach. A Condition Precedent must be complied with strictly. If it is not the claim can be declined in its entirety (whether or not the insurer has been prejudiced by the breach) and there will be no insurance protection, at all.

Every insurance broker should be aware by management of the notification requirements of their own firm’s PI policy.

Notification of PI claims and circumstances
The Claims Made policy brings with it the requirement to notify “Circumstances that might/could/may/is likely to give rise to, a claim.”

The question “what is a circumstance?” is probably one of the most vexing, controversial questions associated with professional indemnity insurance.

A “circumstance” means a circumstance that [might/could/may/is likely to] give rise to a claim. The words “might/could/may/is likely to” are variously used by different insurers and have different practical meanings and there is no uniformity of practice in the PI insurance market. Accordingly, if a broker becomes aware of any reason to fear a PI claim (whether or not such a claim would have any merit) it should take immediate steps to notify PI insurers.

E&O Claims Procedures
Every broker firm needs a clearly defined procedure for identifying, assessing and controlling claims and circumstances that may give rise to a claim.

The chosen procedure must be able to:
- detect and identify potential claims and circumstances as early as possible.
- determine exactly what when and how the matter is reported to insurers.

Why is it important?
Firstly, the earlier a problem is identified and brought under control, the greater will be the chance of minimising its impact and cost.

Secondly, insurers insist upon prompt notification and reporting to avoid being prejudiced by the actions of the client who tries to deal with the matter...
themselves. Brokers are particularly prone to this, in the belief that they can “do a deal” with the parties. Very often they can not and in trying to do so they have caused prejudice to the Insurer, thus entitling them to avoid paying the claim.

Professional indemnity insurers can be less tolerant of members of their own industry than with almost any other Insured, especially of circumstances that are not notified but come to light later.

**When should you notify claims?**
As soon as possible after you become aware.

Every policy of PI insurance required the client to give notice as soon as possible/ practicable of any claim or circumstance which may/might/ could/is likely to give rise to a claim; the expressions differ from policy to policy but the intent is similar. Failure to do so can invalidate the policy cover.

As soon as possible/practicable means just that; without delay.

**What should you report?**
As a rule of thumb, if you have to ask yourself whether a matter should be reported, then consider that it should be. Notify it.

You should report:
- any actual allegation or claim made against you, whether verbally or in writing (and irrespective of whether you consider the claim has any merit, or not);
- any suggestion, intimation or indication that a claim against you is being considered; however remote you believe this to be Notify it;
- any circumstances/situations/problems which you recognise to be a potential difficulty for you or your client or any third party with whom you are dealing;
- any circumstances which could result in dissatisfaction, a complaint, refusal to pay fees or other monies due;
- any other matter that has the potential for becoming a claim, however remote you believe that possibility may be. If it is your case/client that is concerned you are not the best person to make the judgment so refer it to a line manager.

**What about claims which fall within the excess?**
All claims/circumstances should be reported, even those which are likely to fall within your excess.

Failure to do so can lead to a claim being declined.

**Will this affect the premium?**
That is not a matter that should influence your decision as to whether to notify a claim or circumstance.

Insurers tend to increase premiums after a claim, but good brokers can negotiate these things at renewal.

**Anything else I should know?**
Never take a chance with notification of claims or circumstances. Insurers and their lawyers have seen all the excuses and believe none of them.

Brokers who think they know better than the insurers and lawyers usually come off worse. If your firm’s PI is cancelled you are in breach of FCA regulation and must cease trading immediately. That happens.

If in doubt, spell it out – and notify it.
The BIBA PI Initiative offers members help with Professional Indemnity Insurance, related professional risk and PI claims avoidance and management.

BIBA has accredited three, specialist PI brokers to provide access to PI cover which meets the specific requirements of brokers, at competitive terms and rates. Additionally, a team of PI experts is available to provide members with specialist services including risk management, claims advocacy and legal assistance.

**The BIBA PI Initiative enables members to:**
- Obtain optimum insurance protection for its professional liability risks.
- Fully appreciate the risks and obligations associated with being an Insurance broker.
- Avoid breaches of regulation and the duty of care.
- Access specialist support in notifying, managing and negotiating complaints and claims.
- Benefit from an effective approach to liability risk management.

The BIBA PI Initiative has been created in response to feedback from our members and following wide consultation with stakeholders including PI underwriters, brokers, the FCA and the FOS. BIBA is committed to supporting its members in all aspects of broker practice and compliance and welcomes your comments.

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The BIBA PI initiative was a winner of a prestigious Trade Association Forum Award in 2009.
BIBA has appointed three accredited brokers to provide a competitive, specialist resource for members. Each broker is selected for their proven knowledge of professional indemnity insurance and the markets available. The brokers represent both London and regional interests and, between them, a wide range of insurers representing a full cross section of the market.

There is no attempt by BIBA to promise the lowest premium and terms. This is a matter for each member to negotiate with the market but we are confident that the Accredited Brokers have the skill and incentive to serve our members well.

BIBA – accredited PI broker
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Disclaimer
It is important for brokers to appreciate that this guide is not a comprehensive, all-embracing risk management process for insurance broking practice.

This guide is intended for use by members as a risk management tool, raising awareness of the spectrum of risks that have long faced all brokers. It highlights examples of recent PI issues and the role that PI cover might play in addressing those risks.

The information in this guide is provided for general reference purposes only. Whilst every effort is made to ensure that the guide is up to date and accurate, BIBA does not warrant, nor do they accept any responsibility or liability for, the accuracy or completeness of the content or for any loss which may arise from reliance on information contained within the guide.