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DEMANDS AND NEEDS
Tim Goodger and Andrew Stevenson
These notes are derived from a talk by Tim Goodger, partner and Andrew Stevenson, senior associate of Elborne Mitchell, given at Jurys Inn Birmingham Hotel, 245 Broad Street, Birmingham, Bi 2HQ on Tuesday 5 April 2011 relating to aspects of insurance intermediaries' obligations in respect of Demands and Needs.
Where specific reference is made to the law it is to English law as at 5 April 2011.
For specific advice, please contact Tim Goodger or Andrew Stevenson at Elbome Mitchell.

Elbome Mitchell, Solicitors
One America Square
Crosswall
London
EC3N 2PR
Tel: 020 7320 9000
www.elbornes. corn

DEMANDS AND NEEDS
Introduction
The FSA wants brokers and intermediaries to act as "Professionals" in their dealings. In doing so, they are expected to act as professionals and will be judged according to professional standards.
Intermediaries are influenced by the following five main areas when considering their professional duties:
• The Law of Agency
o Common law
o Contract
o Statute/Legislation
o Regulatory (FSA Rules)
There are areas of overlap and these are the aspects that need to be considered in the context of demands and needs. The requirements for a

Demands and Needs statement based on what the FSA Rules require might, at first sight, appear quite straightforward because the Rules are brief and relatively clear. However, when one adds in the need to bear in mind the intermediary's duties to its client as an agent and the requirements of the common law to act with reasonable skill and care in dealings with the client it becomes more complicated. Intermediaries have to have an understanding of what their duties are as agent, and more generally under common law, so that they can assess how best to adapt the requirements of Demands and Needs to their business. And also to assess whether it is something which can be applied in all cases, or whether different policies and procedures are required for different types of clients and different classes of business.

The broker's role — as the intermediary — is that it needs to convey information from client to assured and vice versa, ensuring that each entity in the contract knows sufficient to create a binding contract, where each counterparty' s expectations are met such that they perform their particular parts of the bargain. A fair and accurate presentation of the risk to an insurer is fundamental to that function; and that will turn on the information a broker gathers.

But each impact and feed into the overall approach to be adopted when dealing with Demands and Needs. This shows three things. Demands and Needs is:

1) A fundamental element of your business.
2) Not a prescriptive process.
3) Applies across the practice from contact to contract to claim.

Duties to the client insured/customer

A professional duty owed to a client is an obligation that the professional assumes to the client to take reasonable care. That obligation may be imposed upon the professional in contract or in tort or under the regulatory rules that govern the professional. In order for a claim to be successful against the professional there has to be a duty of care either in contract or in tort which has been breached and loss flows from that breach. The existence of the duty of care depends on the relevant facts and is a question of law.

The role of the broker is generally to act as agent of the insured, acting as expert in respect of insurance and offer services to those seeking the benefit of insurance. The role is wide and includes not only effecting the policy, but also giving of advice on the policies and making claims. The primary duty of care owed therefore is to the assured. The broker must be aware that it may assume a duty to persons who may not ordinarily be deemed to be its client.

Professional standards

The standard by which the professional is judged is against the reasonable skill and care by reference to the members of the profession concerned. Generally, it is for the Court to decide what a reasonably competent broker may do and it is not necessarily what is considered to be an average competence. The general view is that standard is that which, in the opinion of the Court, members of the profession ought to achieve.' The Court is not bound by the fact that a particular profession has a low threshold of competence or operates poor practice. A Court therefore will be assisted by expert evidence, but is not bound by it and may disregard it, leading the Court to make its own assessment of practice. It is therefore not safe to assume that one's own bad practice can be justified and sanctioned by virtue of low standards (actual and presumed) within the profession. The standard that is applied arguably may differ within a profession and those that hold themselves out at specialists may find that the required standards

of competence are higher. The usual approach is to judge a professional against the standard of skill and care appropriate to members of the profession who have the same level or status. It is a fact that standards also change, such that mistakes that may have been considered within the tolerance of reasonable practice may not be.

To whom do these various professional standards apply? And who is potentially affected by failure to comply?

The short test is — to whomever has the intermediary firm or individual broker assumed a liability.

Who is subject of the standards?

• Firms

The FSA rules relating to Demands & Needs apply to "firms". A firm is "(1) an authorised person, but not a professional firm unless it is an authorised professional firm (see also GEN 2.2.18 R for the position of an authorised partnership or unincorporated association which is dissolved)".

An "authorised person" is defined as (in accordance with section 31 of the Financial Services and Markets Act 2000 (Authorised persons)) one of the following:

(a) a person who has a Part IV permission to carry on one or more regulated activities;

See Jackson & Powell on Professional Liability (6t1 Ed.) 2-120, and Midland Bank Trust Co Ltd v Hett Stubbs & Kemp [1979] 1 Ch 384.

2

(b) an incoming EEA firm;

(c) an incoming Treaty firm;

(d) a UCITS qualifier;

(e) an ICVC;

(f) the Society of Lloyd's.

(see also GEN 2.2.18 R for the position of an authorised partnership or unincorporated association which is dissolved.)

"Firms" can mean one of a series of structures, eg corporate structures - limited companies, PLCs, or partnerships or hybrids, limited liability partnerships (LLPs) or sole traders. In most cases, insurance broking/intermediaries entities are either limited companies or PLCs and are subject to the FSA regime. However, certain individuals also will be authorised/regulated in light of their positions.

If the firm has breached its professional standards, then obviously the FSA has the power to take action against it. This includes fines and restrictions on practising.

In actions for breach of professional standards, the common law readily accepts that an individual claimant may bring a claim for damages or some other remedy against a firm, even though it was an employee of that firm that committed the wrong — i.e. the firm is deemed to be vicariously liable for the wrongs of its employees. Since the firm usually has greater resources and — most importantly — more money than the individual, and because the company may have purchased Errors & Omissions or Directors and Officers cover for itself and the benefit of its employees, it is often a much better target for a claimant than suing the individual/employee.

Individual?

Occasionally, a claimant will be so enraged by the conduct of an individual that they will want to sue him or her personally. This of course is possible if

the individual professional is acting as a partner of a partnership, and arguably an employee of a partnership. The partners of the firm may provide an indemnity or may be vicariously liable in addition.
Common law will allow a claimant to sue an individual employee or director of a company for breach of the required standard of professional services. The mere fact that there is a corporate structure in place does not mean that the individual does not or cannot assume responsibility to the relevant individual client or corporate client. Where an individual can be shown to have stepped outside the corporate veil, the individual can be found liable e.g. directors of a company. Thus a report in an individual's name may not necessarily seem out of the ordinary, and indeed some professionals may think it a mark of their own standing, but potentially liability may follow the named person. The issue is whether the individual has been "clothed" by the firm.
See Merrett v Babb2 an employed valuer, assumed personal liability having signed 2 [2001] EWCA Civ 214
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a mortgage valuation which his employer had been retained to provide.
On the other hand, see Williams v Natural Health Foods Ltd3 a director and principal shareholder of Natural Life had not assumed a personal responsibility.
As such, professional standards apply very widely — to both individuals and companies or other business structures. And further, it is a mistake to think that an individual failing to comply will only have consequences for the firm. It can very easily end up being a problem for both the individual and the employer.
The standards that apply
The intermediary operates in a way that brings it within the scope of the FSA regime and common law. The applicable standards for each are as follows.
o Under the FSA Rules
ICOBS deals principally with 'insurance intermediaries' and 'mediation activity'. It is broadly defined and clearly intended to cover the whole industry as far as is possible.
o At Common Law
There is some guidance at common law as to what is meant by an "insurance agent" (commonly someone who is employed by insurers and does not profess to give disinterested advice about competitors products and services) and the distinction with "insurance broker" (someone who acts as agent of the insured for the purpose of effecting insurance policies, holds themselves out as an expert in insurance and gives advice). But generally, the Courts tend not to look at how an individual or firm describes itself, but at the reality of what he or she is doing. So if two individuals produce two identical Demands & Needs statements, both of which are defective, but one calls himself a 'broker' and the other an 'intermediary', it probably will not make a difference to the outcome. The Court will look at the reality of what was being done and by whom. In other words, the substance rather than the form.
An exception might be where an individual describes himself as a 'specialist'. If a party describes itself as having a special degree of expertise over and above that of an ordinary practitioner, that sets him/her apart from others doing a similar job but who are not described as such. In that case, an

intermediary may find that the Courts hold it to a higher standard than those who not describe themselves in the same way. This therefore may have a bearing on the manner in which the broker/intermediary approaches the various components of the retainer and the 'level' or standard which it should apply. Therefore, in the context of ascertaining a client's requirements, it follows that a broker that holds itself out as a goods in transit specialist or a chemical plants specialist or even a catastrophe reinsurance specialist, is changing immediately the way in which the consumer/client (and ultimately the Court) may look at them when it comes to analysing the performance of the retainer.
[1998] 1 WLR 830
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• Insurance activities
o Under the FSA Rules
The ICOBS Sourcebook "General Application Rule" (ICOBS 1.1) applies to
(1) an insurance mediation activity
(2) effecting and carrying out contracts of insurance;
(3) managing the underwriting capacity of a Lloyd's syndicate as a managing agent at Lloyd's;
(4) communicating or approving a financial promotion;
and activities connected with them.
"Insurance mediation activity" is defined very broadly as:
any of the following regulated activities carried on in relation to a contract of insurance or rights to or interests in a life policy:
(a) dealing in investments as agent (article 21);
(b) arranging (bringing about) deals in investments (article 25(1));
(c) making arrangements with a view to transactions in investments (article
25(2));
(d) assisting in the administration and performance of a contract of insurance (article 39A);
(e) advising on investments (article 53);
(f) agreeing to carry on a regulated activity in (a) to (e) (article 64).
"Effecting" contracts of insurance is also defined, as: "the regulated activity, specified in article 10(1) of the Regulated Activities Order (Effecting and carrying out contracts of insurance), of effecting a contract of insurance as principal."
"Carrying out" carrying out contracts of insurance means "the regulated activity, specified in article 10(2) of the Regulated Activities Order (Effecting and carrying out contracts of insurance), of carrying out a contract of insurance as principal."
Both of these latter two relate to acts done 'as principal' which as we shall see is different in the main from where the insurance intermediary is acting as an agent for a principal (i.e. a customer or an insurer).
However the scope of 'mediation' is very broad and, further, the last part "and activities connected with them" aims to make the scope very broad indeed.

So, ultimately, it is very difficult to think of a task that an insurance
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intermediary could carry out with regard to the provision of insurance for a client that isn't going to bring himlher within the scope of one or more of these definitions.

o At Common Law

Again, the Courts tend not to be concerned with labels, unless they have been specifically defined (such as in a contract) and are intended to have a particular purpose. Otherwise, again, the Court will look at what the activity being undertaken actually was and assess whether what was done was below the particular professional standard for that act.

As stated earlier, it is important to review the retainer and consider the duties and obligations of the brokers/intermediary so that one can see how the requirement of "demands and needs" impacts upon the entire retainer and not simply the point in time at which the policy document is sent to the client once the insurance has been effected.

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Principles of Agency

Individuals and companies often act as agents but they or their employees may not necessarily appreciate what that means and have not considered properly what their duties are in that context, or to whom they owe them.

Insurance intermediaries are agents and the key issues are:

For whom are they agent?

What is involved in being an agent?

What is the extent of the duties?

There is also the question of whether the intermediary is an agent for more than one principal. In short, an agent can have a dual agency4 but the agent must be clear what duties it owes and have regard to conflicts of interest, as well as the fact that information that has been received in one capacity may be imputed to another principal.5

It is important to bear in mind here the terminology: one party is an 'Agent' and he/she acts for a 'Principal'.

The Courts determine that a broker is bound by certain duties and obligations as agent. In holding itself out as a professional and with professional standards, the broker is expected to know its duties and to comply with them. It is also important to remember the fact that a party can be a sub-agent of another and indirectly have duties to the ultimate principal.

The general position at common law that an insurance intermediary is an agent of the insured, not of the insurer. Exceptions arise by virtue of risk transfer in respect of handling premium and binding authorities. There are difficulties for agents that have a classic dual agency, such as a binding authority, but also potentially where there are simple agency agreements with insurers or even obligations tucked away in insurers' Terms of Business Agreements (TOBAs) dealing with how the broker must perform.

The crucial point however is the broker, as the agent of the assured once informed of material facts must pass the information on to the insurer.

An understanding of the principal/agency relationship enables the agent to ascertain the obligations it owes its clients and identify instances where it

may not be acting in the client's best interests by doing so.
1) 'Fiduciary' relationship. First and foremost, this includes an expectation that that the agent will put the principal's own interests above his own. For example He/she must:
i) Be loyal to the principal and act in its best interests at all times;
ii) Act in good faith;
iii) Not make a profit out of his position of trust;
iv) Place himself in a position where his and his principal's interests conflict;
Callaghan v Thomson [1999] EWHC 846 (Comm)
Blackburn Low & Co v Vigors (1887) 12 App.Cas. 531
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v) Act for his own benefit or the benefit of a third party without the informed consent of his principal.
Note: fiduciary duties means the general principles that apply to a party acting as an agent. It is also possibly be a 'Fiduciary' with a more heightened form of duty. Amongst the professions, solicitors are Fiduciaries, such that their client accounts are trust accounts in which they regularly hold money for clients. Liquidators, receivers and administrators owe Fiduciary duties. Auditors ordinarily do not. Promoters and directors owe fiduciary duties, this time to the company itself, although not to individual shareholders unless the shareholders acting as a body can direct the company to enforce the duties. And the Companies Act 2006 has now codified directors' duties, including their fiduciary duties. Intermediaries too will be classed as owing some Fiduciary duties since January 2005 their client money accounts are held on trust — albeit one which gives the intermediary firm wide latitude and expressly excludes an obligation to account for interest or other investment return on funds held.
2) Duty of confidentiality. This is to some extent an element of the fiduciary duty. An agent is expected to keep confidential any and all information given to him by his principal in connection with his role as agent. Further, there is a duty not to use that information other than for the purposes for which the intermediary has been instructed: i.e. to advise and place insurance on behalf of the insured. This is not often a problem where there is a single insured for whom the broker acts, but might be if a broker acts for a number of similar businesses and, in the course of acting for one, learns information about one which is relevant to the insurance requirements of another. This gives rise to important points when dealing with various entities within a group and the persons with whom the brokers liaising when being asked to advise on the insurance of the overall group. To whom do his duties lie? Is the knowledge/information gained general knowledge in any event and from whom has the information been obtained? The broker has to make clear at an early stage what it is doing and for whom.
3) Duty as regards client documents. An agent has a responsibility with regard to his principal's documents. So, where after an insurance policy has been placed and has incepted (the insurer says it has mislaid a copy of the documents it was shown on placement and asks for another copy) or asks to see a document (that was not shown at placement but that is referred to in another document that was shown to it), can the broker just hand over a copy? In light of the duty of disclosure to the insurer and the duty of good faith the broker should seek the specific instructions of the principal/insured. The broker should advise the assured of its duties to the insurer and the consequences of not performing them. If the insured refuses, the broker should consider with the insured what to tell the insurer as to why the request is refused.6

In North & South Trust v Berkeley7, a Lloyd's broker found itself holding a loss adjusters' reports which the underwriter bad instructed him to obtain (in accordance with the then prevailing practice at Lloyd's). The insured client insisted on seeing the reports. It led to a legal dispute. The judge had to decide the divided loyalty point. He explained the principle:
"Fully informed consent apart, an agent cannot lawfully place himself in a position in which he has a duty to another which is inconsistent with his duty to his principal".
6 Broker duty under s. 19 Marine Insurance Act 1906
7[1971]1WLR 470
8
4) Brokerage/Duty not to make a secret profit. Brokerage is properly a sum paid to the broker by the insurer, not by the insured. It is classed a commission paid by the insurer for bringing the business to it.8 For administrative reasons, it is usually deducted from the premium paid by the insured and the net amount is passed on to the insurer, but strictly the whole amount and should be paid over and the insurer refunds the commission. There is a general duty on an agent not to make a secret profit and so generally an agent is required to disclose to its principal what profit it has made by virtue of the agency relationship. That, of course, raises difficult questions of whether an agent is entitled to know, how much 'profit' the agent is making as that may be highly commercially sensitive information. The more modern common law view is that an agent is obliged to account for any profit in excess of 'normal' brokerage that he has earned in his capacity as agent9. Though that brings with it questions of what is 'normal' profit. That will normally be determined by regard to market practice for a particular type of insurance transaction and, if necessary, by the use of expert evidence.
Exceptions to the general rule
When the broker is acting under a MGA / Binding Authority / Other Structure it may well be an agent for both the insurer and the insured and will likely owe duties to both. These include a dual duty of care, duties of disclosure, confidentiality, document management, accounting etc. The intermediary acting as coverholder undoubtedly owes a duty to the insurer to act with reasonable skill and care. ? CANOPIUS?
In Woolcott v Excess Insurance Co Ltd'° the broker effected home insurance for the claimant under a binding authority granted to them by the defendant insurers. The brokers knew that the claimant had a serious criminal record but failed to pass on the information to the insurers. Following a fire, the insurers discovered this and denied coverage on the ground of non-disclosure. That failed because the insurers were deemed to be fixed with the knowledge that the brokers had because they were acting as the insurers' agent. So the claimant was successful. However, in separate third party proceedings the insurers secured an indemnity from the brokers on the ground that the brokers had failed to pass on the information to them.
NB. Very often there will be some form of written contract/agreement between the insurer and the broker that governs what each is obliged to/not do (being another TOBA). In signing up to this, the intermediary ought to have regard to the interests of actual and potential insureds so that the intermediary is not going to repeatedly find itself in a position where its duties conflict."
Can a broker act in the best interests of both insurer and insured simultaneously or will there always be a possibility of a conflict of interest? The answer is that a conflict in itself is not a bar to acting for both parties — there is an obligation to a client/customer to advise it if a conflict has or may arise, but — with having been provided with all of the necessary information — it is open for the client/customer to consent to the proposed activity

notwithstanding the actual or potential conflict. The important thing is to recognise that duties are owed to both parties and to seek
Pryke v Gibbs Hartley Cooper [1991] 1 Lloyd's Rep 602
Chan v Zacharia [1984] 154 CLR 178
10 [1978] 1 Lloyd's Rep 633
Goshawk Dedicated Ltd v Tyser & Co [2005] Lloyd's Rep JR 379
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instructions if a conflict does emerge.
Dual agencies are possible and often arise in the insurance market'2 and are permissible, but under the law of agency there has to be informed consent on the part of the relevant principals.
With this in view, therefore, the ascertainment of the demands and needs of the client assured are perhaps clearer in that the client's demands and needs are to be at the forefront of the agent's mind. There is a need to ensure that where there are instances of dual agency, where the broker may act as agent for the insured but also acts as agent for insurer (either through an agency agreement or under a delegated authority from an insurer, by which the broker may receive an overriding commission), the broker must ensure that the client's demands and needs are first and foremost.
12 Callaghan v Hedges [2000] Lloyd's Rep. JR 125
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The Common Law Duty of Care
Duty to act with reasonable skill and care
The common law has long since implied a duty on an intermediary to act with the skill and care expected of a reasonable intermediary when carrying out business. The problem comes in interpreting what this seemingly woolly phrase means in practice. The starting point is usually to consider what were the duties owed by the intermediary and to whom and whether they were they breached.
o Duties
The duties owed by an intermediary to the customer can be express and/or implied, and owed in contract and/or in the tort of negligence. The duties in contract and tort run concurrently. Additionally, implied duties exist in statute, such as under the Supply of Goods And Services legislation.
Ordinarily, it should be possible to ascertain the duties by reference to the terms of the retainer, which may be expressed in written terms, as well as common law and practice. Written terms may be contained in a TOBA between the intermediary and its customer, including key terms that an intermediary is obliged to disclose, such as commission and the analysis of the market. A court considering the existence of a duty and the extent of the duty may have to resort to expert witness evidence - usually an experienced insurance intermediary.
Primarily following the decision in Youell v Bland Welch (no 2)13, an insurance intermediary has four main duties:
1. ascertain the client's insurance needs;
2. ensure a proper presentation of the risk to the insurer
3. take reasonable care to ensure that there is a enforceable contract of insurance that accords with the client's requirements;
4. inform the client if insurance cannot be placed in accordance with the client's needs.

In order to comply with these duties the broker needs to ascertain sufficient information and instruction from its client, such that at each stage the broker is able to say that is has satisfied the obligation. The broker needs to advise therefore on the duty of disclosure that the insured owes the insurer, and advise the insured on materiality of matters.

It follows that each of these four duties require the client to recognise the customer's needs'. There is an interchanging in the case law of the words "need" and "requirements". That shows the concept is not simply the client's intention or want to obtain an insurance, which perhaps equates with the demand the assured makes for insurance, but a wider obligation to seek out what insurance suits the client; the insurance should meet the customer's requirements. Although an intermediary cannot always place insurance for the risk, it must advise the customer if it has not been able to do so. In other words, the broker is obliged to

13 [1990] 2 Lloyd's Rep 431

make clear that it has not been able to meet the requirements. Therefore not only has the broker to ascertain the demands, it needs to be satisfied that those have been satisfied. Failure to inform the client that it has not been possible to satisfy the demands, either because the coverage cannot be obtained in the market on the terms that would be required, or that the market is not able to provide those terms at the price that the client is prepared to pay, nonetheless constitute a breach of duty because, without the information, the insured is unable to make alternative arrangements. There is in effect a loss of opportunity for the client (because there has been a failure by the broker to properly inform the client of the true position), thus giving rise to a potential cause of action against the broker.'4

An inability to place insurance on terms required by the customer does not enable an intermediary to justify placing a policy on any terms, without any reference to the customer. There may be exceptions where there are limitations on the time available to place the risk. In light of the electronic communication age the intermediary likely can seek instruction from the customer.

The broker's role to ensure that the insurance that has been obtained meets the client's requirements necessitates the broker actively considering whether the insurance could or should have particular clauses and whether the wording in the policy actually provides the extent of cover that the assured requires for its particular circumstances. This may give rise to harsh consequences, in that the customer may in reality require insurance that is readily available, but it does not ask the broker to obtain that.

There may be instances where particular clauses should be in the wording and this needs to be considered by reference to market standards and whether the client's needs are such that the broker should ascertain if the additional cover can be obtained at all. If it can be obtained for no additional premium/cost, and yet the broker does not obtain that cover, then the broker may be criticised for not having obtained the cover. This, in part, will turn on the extent the potential assured informed the broker of the risks in its business and, in part, what risks to the business a broker ordinarily would be aware of and for which insurance may be obtained. The broker therefore has to be on enquiry and ascertain the foreseeable risks to the prospective assured, be it a business or a domestic insurance. If the additional cover is available, for additional premium but the broker does not obtain the client's further instructions, then the broker likewise may be criticised.'5

If the broker is aware that the client has obtained a particular form of cover previously or that the broker is aware that a particular event has arisen (which did not, but may give rise to a loss) and that a similar event may occur again, then the likelihood is that the broker would be aware that cover

of this type is required in the future. Failure to obtain that coverage is therefore likely to be a failure of the broker to obtain insurance that meets the client assured's demands and needs. In addition, there may be a failure to ascertain the demands and needs through a lack of enquiry or seeking to obtain proper and full instruction.

Where a clause is customary, then the broker should seek to obtain it if there is no additional cost. E.g. where the cover is for mortality cover for livestock, should

" Allied Maples Group Ltd v. Simmons & Simmons [1995] 1 WLR 1602, case against a firm of solicitors. See - Harvest Trucking and Co Ltd v Davis T/A PB Davis Insurance Services [1991] 2 Lloyd's Rep 638

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that have included theft cover? Answer — no. 16

However, there is always an issue as to what is the extent of the retainer and what is the broker being asked to do? A restricted instruction does not necessarily result in absolving the broker to undertake certain aspects of the demands and needs analysis.

Duty to advise on policy

Where the broker does not advise the client on certain terms which impact upon the cover in such a way that they limit or curtail the cover then it is arguable that the broker has failed to ascertain the clients' demands and/or needs or indeed it has failed to obtain adequate or sufficient cover to meet the demands or needs.

Ambiguity

Where the client's instructions are not clear then it can reasonably be said that the broker may not have ascertained the demands or the needs of the client. Therefore, if there is ambiguity in the instructions and the intermediary in error places an insurance which is insufficient or limited, then it is the intermediary that will likely be liable to the customer for the resultant loss. In order to satisfy the obligation, the broker does need to ensure that the instruction is understood, although there may be instances where the client itself may be ignorant of the extent of the cover it needs, or is available. The level of the client's knowledge therefore is something the broker should consider and ascertain. This is because a Court likely will take into account that level of knowledge when ascertaining whether the level of cover obtained was sufficient.

When in a chain

Although there is no contractual nexus between a placing broker and the client where there is a producing broker intervening in the broking chain, the placing broker equally has a duty to ensure that it understands the instructions from a producer and to check the underlying client's needs.'7

Security

The intermediary is obliged to test the market, but is not obliged necessarily to obtain the cheapest price for the insurance, since the price needs to be considered in the context of the insurance, the terms, the security and in part any prior relationship with the insurer, such as at renewal.

The security for the insurance, on the face of it, may not seem strictly to relate to demands and needs, but it goes to whether the insurance is adequate and meets the client's requirements, particularly at common law (where ascertaining a client's demands applies arguably to reinsurance and large risks insurance, which otherwise might be excluded under the ICOBS). The issue of security often only comes to the fore on insolvency (administration or liquidation of the insurer). Although an individual private customer will have recourse against the FSCS in particular circumstances,

and the overall sum payable to the client may be up to
16 See O'Brien v Hughes-Gibb 1995 LRLR 90.
' Fisk v Thornhill & Son [2007] LRIR 699, case dealing with terms of new cover on a renewal — See Appendix 1
13
90% of the claim, there remains a risk that the assured seeks the shortfall (where significant) from the broker. For commercial businesses, redress to the FSCS is not available save where there may be partnerships.
However, a broker may have a liability if security is poor (see Osman v Ralph Moss (1970) - English locus classicus). Mr Osman was a cabinet-maker whose ability to read and write English was limited. His brokers placed his motor insurance with Belvedere Motor Policies, a company known in the trade at the time to be in financial trouble. Shortly after the policy incepted, a winding up order was made against Belvedere and the brokers sent a rather woolly letter to Mr Osman suggesting he insure elsewhere. He had no idea what was going on, until he had an accident and was fined £25 for driving whilst uninsured. The brokers were found liable for his loss.
An Australian authority: Lewis v Tressider Andrews Associates (1987) suggests that a broker has a continuing duty to advise the client if the broker learns of any information which indicates that the insurer might not remain financially sound.
Lewis was a Queenslander fisherwoman who went to her local brokers for cover for her fishing boat. They went to the Lloyd's brokers Oakeley Vaughan. At the time, the Lloyd's market was not particularly interested in Australian fishing risks, but Oakeley Vaughan managed to find someone who would write it; the Old Charter Insurance Company, a company which had recently been set up in the Turks and Caicos islands and from its inception, had acquired assets of over $9 million which were invested mainly in property. According to its business plan, it expected to realise nearly $2 billion from its investments in 10 years. Oakeley Vaughan sent the Australian brokers copies of the financial information, including a copy of Old Charter's balance sheet, from which it should have been obvious that Old Charter was a sham. The brokers however took it at face value and Mrs. Lewis was signed up.
Oakeley Vaughan became aware of the Old Charter and sent the Australian brokers telexes warning them that there were problems about its solvency. The brokers however ignored the warnings; Mrs. Lewis's boat caught fire one evening and Old Charter could not be found.
The Court concluded that "as long as the relationship of broker and client exists, there is a continuing duty of care"; therefore, if the security looks in danger half way through the coverage period, the broker has to bring this to his client's attention.
These facts are extreme, but it illustrates that brokers should not automatically assume first, that security is not of great importance and second, their job is not complete after placement.
o Has there been a breach?
Having established that a duty exists, the question will be — has that duty been breached? That is established by reference to the skill and care of the reasonably competent intermediary in the particular aspect of the market or specialism, which is the subject of the claim. Again, expert intermediaries are frequently called upon to give evidence as to what is "reasonably competent" in that area.
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The question of whether there has been a breach of the duty will be considered in the context of the insurance obtained and whether it satisfied the demands and needs of the client will be judged on the facts of the circumstances, what coverage was obtainable in the open market and whether there were any limitations to the obtaining of the cover, for example a time stricture which meant that there was little time to carry out proper analysis of the market, or to approach other insurers, or to negotiate the required cover.

Has damage flowed from the breach?

There can be no valid claim in common law against the intermediary if no damage has flowed directly from the breach of duty. To establish the nature and extent of damage the claimant will be required to provide evidence of the damage caused. This will be achieved by reference to monetary losses because the insurance policy relied upon has not met the losses or damage/es suffered by the customer/claimant.

o How does the intermediary know or judge what is suitable?

The intermediary is expected to know sufficient about the nature and extent of the insurance policies offered to the client and to know the pros and cons of those policies from a combination of their qualification, training, general experience and the knowledge and skills of the peer group in which they operate.

The basic test is - how another competent intermediary would or would not have advised or acted in the same situation?

As set out above, if an intermediary holds itself out as specialist in a particular field of insurance then the duty will be measured against another similarly specialist intermediary in the same field. A buyer of a product from an intermediary advertising itself as a specialist is entitled to expect advice and services commensurate with what can be reasonably expected of a specialist in that field of expertise.

o To what should the intermediary direct their mind?

Insurance policies are structured in a broadly similar way in most classes of insurance business.

o Insuring Clause

• Exclusions from cover

• Conditions of cover

• Conditions precedent to cover

o Claims notification provisions

• Warranties

The policyholder is NOT an expert on insurance (unlike an intermediary who is deemed to be such) and it is reasonably foreseeable to an intermediary that many

policyholders will not understand the policy terms and expressions to their fullest extent and meaning. Whilst it may be no defence for a policyholder to claim that they had not read the policy (so as to understand their obligations and the scope /limitations of cover) it may be a reasonable stance for them to take when bringing a claim that they did not appreciate the scope and implications of those terms and of any obligations under the policy with which they are not familiar.

For example, most policyholders would not be expected to understand the difference between a condition and a condition precedent. It will need

explaining to them. Some policyholders may not understand the condition of average or the implications of warranties, for example. It is certainly the case that those businesses familiar with company law will think a warranty in an insurance policy has the same meaning, when that is not the case. Those policyholders less familiar with the English language may be at a further disadvantage and it is arguable that the intermediary should have this in mind also, and take suitable steps to inform the policyholder of the things of which they must be aware.
These duties arise not only when a policy is first effected but also at the time of each renewal (which in law is not actually a renewal of the old contract but an entirely new contract).
Duty of Disclosure
Intermediaries will be familiar with the duty of disclosure; that it is a complex area of insurance that cannot be addressed in great detail here. However, the intermediary must advise the proposer about its duty of disclosure to insurers and take reasonable care to elicit information that the insurer will require and should reasonably expected to be told. The courts have held that an intermediary is under an obligation to ensure that the customer understands and appreciates the extent of the duty of disclosure and recognises what is and what is not a material fact. There is an inter-relationship between what is material, what must be disclosed and the extent of the cover being provided.
Materiality, as it is often referred to in the insurance industry, is a foreign topic to anyone outside the industry. That and the doctrine of utmost good faith is too complex a subject for the average purchaser of insurance. Every intermediary would be expected to realise this and make a particular effort to help the proposer to comply with material disclosure as the intermediary knows its intent and importance. The intermediary is under an obligation to ensure that all material information necessary to comply with the duty of disclosure is passed to the insurer, although the intermediary does not have to act as detective, it should probe where necessary. This will apply not only on an initial dealing with the customer, but also on a renewal.
The drastic consequence of the insured breaching its duty of utmost good faith owed prior to the conclusion of the contract of insurance, and the avoidance of the contract ab initio means the broker not only must ensure it understands the duty but also that the consumer! assured does too.
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The duty of utmost good faith is the basis of both non marine and marine insurance contracts and it applies pre-and post contract:
o disclosure of material circumstances (by the assured) [s.l 8 MIA]
duty to disclosure (upon the broker) [s. 19 MIA]
o duty not to misrepresent material matters (either by the broker or the assured) [s.20 MIA]
The requirement is for the insured to disclose every material fact “known to the assured, and the assured is deemed to know every circumstance which, in the ordinary course of businesses, ought to be known by him....” s.18(1) MIA 1906.
The law therefore assumes that the insured will know the facts relating to the risk to be insured, because it is those facts upon which the insurer will base the decision to insure. [n short the underwriter is induced to enter into the contract on the basis of representations by the assured — through the agent! broker.
NB. Many claims against intermediaries are based upon their failure to inform the proposer about materiality and there is very little defence that can be advanced, in most cases.

o Limits of advice

There are limits, however, to what an intermediary is expected to advise upon. For example, an intermediary's duty includes advising on the sum insured or the limit of indemnity but that does not require the intermediary to act as a valuer. However where the intermediary assumes a broader duty by giving a valuation or offering legal advice (over and above that usually expected of an intermediary), liability may attach if the intermediary breaches that broader duty. Nonetheless, in the context of demands and needs, adequate understanding of the extent of the coverage and the overall limits of indemnity are fundamental not only because it impacts on the business should it suffer a loss, but it may impact also upon the cost of purchasing insurance and therefore the business overall. Understanding what the business or individual client is able to afford and what the client understands is available falls squarely within "demands and needs".

The duties of an intermediary include guiding the proposer or the policyholder as to the scope and nature of cover, obligations, conditions and exclusions and a failure to use reasonable skill and care in doing so could be a breach of duty of care, in itself.

Contract

Principally, contract has been the way in which the Court have exercised control over the standard of performance of the broker, since the broker enters into a retainer with the client, an agreement, by which the broker agrees to provide services to the client and in respect of which the broker will be remunerated, albeit by way of commission usually although it is not uncommon for the services to be provided in return for a fee to be paid by the client. This gives rise to express and implied terms in the contract. The requirement (albeit imposed by the regulator) to use Terms of Business Agreements ("TOBAs") means there are express

terms as to what the broker will do and how it will perform certain aspects of the task. TOBAs differ and there is no standard document although market associations have provided templates. Brokers have tended to adapt these to comply with their own business practices.

Contracts or TOBAs with customers or insurers, likely contain a self-imposed (express) obligation on you to perform a defined set of 'Professional Standards'. The broker agrees to comply with the terms, even if they are more onerous than the statutory obligations and/or common law. In effect, non-compliance with the written standard (level) or the non-delivery of a particular outcome would likely result in a breach of contract, which would be actionable in damages.

In addition to these are implied terms.

The common law position and the rules relating to agency may be cemented, varied, widened, restricted by the broker/intermediary, by making clear the terms of the retainer. The common law duties described can be varied orally or in writing, so that each contracting party knows, understands and agrees what is to be done, how it is to be done, by whom, when and for what price.

The broker must be sure to identify who is its client. This may seem obvious, but it is possible for various different parties to have interests in the same property and risks.

TOBAs are a fundamental part of the business relationship between a broker and the client although retainers in the past have been oral contracts, the advent of professionalism, regulation of brokers under the IBRC, Lloyd's and subsequently the GISC have resulted in the broker reducing the terms to writing (or at least the basic terms on which it will act), such that the client/assured has a written contract. This does not necessarily set out all the

broker/intermediary obligations but certainly sets out some and may be used to finesse the common law duties discussed. Brokers often fail to obtain signed copies of the TOBAs they have sent to counterparties and that failure is the first step to the broker being unable to prove what was agreed. The broker should record what it is, it is being asked to do.

By setting out in a TOBA the terms upon which the broker will act, the broker sets out in contractual form the duties that it owes to the client. These duties may include a statement of some of the service levels the broker will provide, the common law duties covered, and/or it may include additional contractual duties, which increase the broker's obligations or even the standard that the broker would otherwise be obliged to meet. In essence, the retainer may have greater breadth than it would otherwise.

A TOBA may also set out the information that a client is obliged to give the broker in order to assist the broker in the giving of advice and performing its obligations. For example, the client might agree to provide timely instruction, if that can be defined, or it may require that client particular information about a risk. It is important, however, that when the TOBA is provided to the client important terms are highlighted and in some circumstances that the terms are discussed.

Many brokers provide clients with information sheets relating to the obligations a client has towards an insurer including the duty of disclosure. Although those information sheets do not necessarily become a contractual term — and it likely would be somewhat burdensome to include those as a term — information sheets enable parties to convey information about duties and obligations of the parties when entering into an insurance contract. Such standard documents, may be useful to clients, but can also be formulaic and as a consequence, general and inappropriate. They may merely deal with part of the broker's obligations and may not

necessarily satisfy them entirely. As well as providing information, they also (providing that a copy is kept on the broker's file) assist in demonstrating what advice has been given. That can be important when it comes to dealing with complaints and claims. However, in order for a client to understand its duties and the broker to be satisfied of that, more has to be done than despatching documents. The content of the documents have to be satisfactory, clear and provided at the appropriate juncture.

There is a question as to how a broker conveys to a client that the broker has certain relationships with insurers, such as binding authorities and that the search for a product may not be exhaustive. Whether the broker does so orally, or makes this part of the retainer by formally referencing it in the TOBA is a moot point, but whatever the position, the broker should ideally convey that it will not be approaching all insurers in the market place, nor that the broker knows of all the insurance products in the market place. Not only should that information be conveyed to a potential client but the client should acknowledge the position. The client's awareness of the limitation of a broker's researches goes to the heart of the retainer.

It is a common problem in commercial arrangements/contracts, and often gives rise to disputes, that the terms and terminology between documents are not consistent. This gives rise to a tension between them. These inconsistencies can mean that when a dispute arises, it is difficult to reconcile the two, and may result in a counterparty being able to argue successfully that the other was obliged to perform a particular function or task. Equally, ambiguous wording or badly phrased clauses similarly can lead to dispute. The difficulty for the professional is the risk a Court is likely to be more inclined to find favour with/prefer the evidence of a consumer/claimant that rarely purchases insurance or that is not familiar with wordings or phrases or insurance terminology than the professional that deals with such matters on a daily basis.

A review of the TOBA to be used for clients for particular classes of businesses and the documentation provided to them, as well as D&N Statements, is an essential element of risk management. These are the main documents (apart from policy documentation) that a broker will provide to a client. The provision of documentation will not discharge the broker's obligations in each and every circumstance.

Different TOBAs

Different clients

It is not uncommon for brokers to have one TOBA for all commercial business clients and one for consumer clients. There may be instances when that "one size, fits all approach" is not appropriate, and the assumption may be that the "average consumer" or purchaser of insurance will have a particular level of understanding. For example, the broker may assume that a risk manager within a business is au fait with insurance terms and the extent of coverage available, as well as the broker's role.

TOBAs could be supplemented therefore by appendices for different clients and also for different business types.

The generic TOBA — which sets out what the broker will do — and also to an extent what the broker requires — is a starting point.

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Different Business

There is good reason why different TOBAs should be used for different business. There may be different obligations for the client; different matters, to be considered. Although not all aspects will be different — and there will be common standard clauses, the broker by looking at each type of business in turn will look at its processes and amend the TOBA to reflect/conform with that.

TOBAs — a means of limiting risk/liability

Terms — excluding liability

The terms of the retainer are key in setting out expectation and specific obligations and duties.

A party might seek to exclude particular breaches e.g. negligence, as well as types of loss e.g. indirect and consequential losses or economic loss, as well as the extent of the loss for which it may be found liable. This may be expressed in different ways — express retainer of objectives: a statement as to what the broker will be liable for and excluding all other aspects OR express retainer of aspects for which the broker will not be liable: a statement as to what is excluded.

The general approach should be that an exclusion of liability is express, clear and unambiguous and brought to the contracting parties' attention. N.B. contra proferentem rule

— i.e. ambiguities will be construed against the party trying to rely on the contractual term(s). If the intention is to exclude negligence then that has to be in clear language.

BUT, there is authority to say that it is not acceptable for a professional to exclude liability for negligence: see Smith v Eric S Bush'8.

Are all limitations enforceable at law?

The question as to whether a clause is enforceable depends on whether it is reasonable in the context of UCTA 1977 (s 2(2)) and The Unfair Contract Terms Regulations 1999.

UCTA 1977 - question of reasonableness will turn on a number of variables including:

- The negotiating strengths of the parties;
- Whether the consumer was made aware of the limitation/restriction in the terms;
- The overall liability/potential liability of the broker, considered in the context of the overall fees earned by the broker;
- The extent of the professional indemnity insurance that the broker has taken out e.g. quantum of cover.

See reasonableness UCTA 1977 (s 11):
- Fair and reasonable in the circumstances
- Knowledge of the parties (actual or constructive)

18 [1990] 1 AC 831

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- Bargaining position of parties: strength
o broker/individual
o broker/commercial entity
- Inducement to agree to term
- Opportunity to engage another
- Knowledge
- Exclusion of a condition and whether in the circumstances that is reasonable. Care in drafting the terms of retainer

The way in which the retainer is drafted will seek to exclude the potential for wider liability. Careful statement of what is to be undertaken and by whom (either by the broker or the customer) will enable ascertainment of the responsibilities during the course of the business relationship and of the parties' duties in the event of a dispute. This may mean that the customer not undertaking a critical aspect might lead to relief of liability for the broker. See above however with regard to the assumption of responsibility that may still arise after terms have been agreed i.e. terms can be varied by conduct. Where that arises a broker will owe the same duty of care that he/she would have owed in any event.

Exclusion of liability to third parties

The difficulty in trying to exclude liability to third parties is that third parties may not have notice of the exclusion, and nor are they party to the contract. — See doctrine of privity of contract.

It is important therefore to identify who is the customer, who will rely on the advice given and in what capacities are other parties acting.

Statute/Legislation

Statute impacts upon the extent of the duties owed by the broker and attempts to limit those duties.

(1) Supply of Goods and Services Act 1982

Requires a supplier of a service acting in the course of business in England, Wales and Northern Ireland to carry out that service with reasonable care and skill and, unless agreed to the contrary, within a reasonable time and make no more than a reasonable charge.

(2) Unfair Contract Terms Act 1977

This relates to transactions between businesses. In general, businesses are assumed to be free to enter into whatever contracts they agree between

themselves However, UCTA places a number of restrictions on the contract terms businesses can agree to. Specifically, it lays down rules for the ways in which vendor

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businesses can use exclusion clauses to limit liability in certain areas (e.g. excluding liability for death or injury is not permitted in any circumstances; excluding liability for losses caused by negligence or for defective goods is permitted only if it is reasonable).

(3) Unfair Terms in Consumer Contracts Regulations 1999

This protects consumers against unfair standard terms in contracts they make with traders. The Office of Fair Trading, together with certain other bodies, can take legal action to prevent the use of such terms. The UTCCRs can protect consumers from terms that reduce their statutory or common law rights and from terms that seek to impose unfair burdens on the consumer over and above the obligations of ordinary rules of law.

The Regulations apply a test of fairness to all standard terms (terms that have not been individually negotiated) in contracts used by businesses with consumers, subject to certain exceptions. The main exemption is for terms that set the price or describe the main subject matter of the contract (usually known as 'core terms') provided they are in plain and intelligible language. The Regulations thus apply to what is commonly called 'the small print' of standard form consumer contracts.

A standard term is unfair 'if contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer'— Regulation 5(1) of UTCCR. Unfair terms are not enforceable against the consumer.

(4) Contracts (Rights of Third Parties) Act 1999

This provides, amongst other things, that a party who is not named in a contract (including an insurance policy) may still have the right to bring a claim in respect of a breach of an obligation in that contract if the contract confers a benefit on them in respect of that obligation. Therefore a party to a contract of insurance may bring a claim against an insurer even though there is no contractual relationship. The parties to the contract may, however, expressly agree to exclude any third party or named parties from any rights under the relevant contract.

(5) Limitation Act 1980 / Latent Damage Act 1986

These specify the time limits in which parties have to make claims for breaches of contract or claims in negligence (including challenging a decision by an insurer to refuse to pay a claim or avoiding a policy).

These legislative provisions therefore impact upon the relationship between the intermediary and the customer and, in turn, the binding nature of the terms. Ultimately, that goes to whether the broker is obtaining the insurance that the insured requires or whether the scope of the broker's retainer (and duties) is either limited or the terms are unduly onerous thereby putting in question whether the intermediary has effected his/her instructions and met the client's requirements.

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Regulatory

The FSA Handbook (the special section of 'Business Standards' devoted to insurance; the ICOBS Insurance: Code of Business Sourcebook).'9

Eight sections: Application; General Matters, Direct Communications; Information about the firm, its services and remuneration; identifying client needs and advising; Product Information; Cancellation; and Claims Handling.

The Application Section (Section 1) deals with who the regulations apply to and the types of insurance work it covers. The activities of nearly all insurance brokers is such that they fall under the regulation of the FSA undertaking a "regulated activity" within the meaning of the Financial and Services Markets Act 200 ("FSMA"), simply by virtue of their arranging the purchase of insurance policies (including introducing a customer to an insurer or insurance broker), advising on insurance policies (including recommending a specific insurance policy to a customer), dealing as an agent (including entering into a contract of insurance with a customer on behalf of the insurer (for example, the issue cover notes) or vice versa.
A breach of the rules by an authorised broker is actionable at the suit of a private person (being an individual unless he suffers the loss whilst undertaking a regulated activity) who suffers loss as a result of the breach.
In the same way as we have discussed how the general retainer, and the common law duties may be varied (within reason and in particular statute), the FSA regulatory regime impacts upon the retainer. The FSA by its rules have imposed further (statutory) obligations upon the regulated entity, stipulating what the regulator expects the insurance intermediary/broker to do. This is in simple terms, just another layer of duties or obligations that the regulator considers to be necessary in order to comply with its statutory objectives in particular Consumer Protection and Market Objectives. Therefore, the FSA rules/regime impact upon the professional standards to which we referred earlier. The Rules can be used as a measure or standard by which the intermediary should perform.2°
The FSA' s requirement relating to Demands and Needs are contained within Section 5 of ICOBS. Under section 5.2.2 an intermediary:
(1) Prior to the conclusion of a contract, a firm must specify, in particular on the basis of information provided by the customer, the demands and the needs of that customer as well as the underlying reasons for any advice given to the customer on that policy.
(2) The details must be modulated according to the complexity of the policy proposed.
There are various additional requirements:
(1) A statement of demands and needs must be communicated:
(a) on paper or on any other durable medium available and accessible to the customer;
19 http://fsahandbook.info/FSA1htm1/handbookJ1C0BS
20 See Nicholas G Jones and (1) EnvironCom Limited (2) EnvironCom England Limited —and- MS Plc tla Miles Smith Insurance Brokers [2010] EWHC 759 (Comm) para 53 "Broker's duty".

(b) in a clear and accurate manner, comprehensible to the customer;
In addition, to ICOBS, the FSA also requires the broker to know about and practise the obligations of their Treating Customers Fairly initiative (TCF)21. Since December 2008 firms have been expected to be able to show to the FSA and to themselves that they have been treating customers fairly. This involves complying with the six stated Outcomes of the initiative.
Of those six, three are relevant to the obligations of Demands and Needs.
Outcome 3: Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale.
Outcome 4: Where consumers receive advice, the advice is suitable and takes account of their circumstances.
Outcome 5: Consumers are provided with products that perform as firms have led them to expect, and the associated service is of an acceptable

standard and as they have been led to expect.
There is a considerable cross-over of the language therefore between the wording in Section 5 of the FSA Handbook and under TCF. So, the position ought to be that if you are carrying out your Demands and Needs obligations properly, then you should also be able to demonstrate that you are going a long way to showing that you are TCF compliant.
In some respects, Demands and Needs is merely the FSA requiring intermediaries to adopt a form of best practice that is adopted by other professionals with regard to collecting information from clients and providing advice to them. The intermediary is required to seek information from the client in order that the intermediary can ascertain what that client's demands and needs are and then record what those demands and needs are in a statement for the client's benefit. Having done so, it should give the intermediary a solid platform on which to determine what his/her advice to the client is going to be about the product that is suitable for that client. Again, the intermediary is required to specify the underlying reasons for the advice that has been given so that the client can understand the thought process that led to the decision. And the statement should obviously record the advice ultimately given.
Assessing Demands and Needs under the Regulations
The ICOBS regulations require the intermediary to take specific action with regard to assessing the proposer's Demands and Needs and this is in addition to the common law duty to exercise reasonable skill and care in the exercise of its business.
Specifically, the intermediary is required to elicit information from the proposer that ensures that the insurance cover sold by the intermediary is suitable for the risks to which the proposer (proposer's business) is exposed. The insurance should meet the customer's requirements. 22
Documenting the intermediary's thought processes should hopefully enable the intermediary to produce better advice, more specifically targeted to an individual client's actual (rather than presumed) demands and needs. Also, in the event of a problem about the product/coverage, it will provide the intermediary with evidence to show that it acted
21 http://www. fsa. gov.uk/Paes/Doing/Regu1ated/tcf7index.shtm1
22 ICOBS 4.3.1

appropriately, which it can then use in defending the claim. A contemporaneous written record is usually far better evidence than an individual's often hazy recollection of something that may have occurred many years previously.
The intermediary must address two separate and distinct aspects: the collection and then the collation of data/information. One thing is clear - gathering information to assess Demands and Needs is a task that requires sufficient diligence, both to obtain the information volunteered, but also to work out whether this in itself requires other information to be elicited which, in the intermediary's reasonable judgement, is necessary to form part of the assessment of D&Ns.
In order to provide an accurate D&N statement, ideally the intermediary should ensure:
° accurate data/information is obtained from the customer;
o it has sufficient information to make an assessment;
o that the information is correctly processed and applied; and

o it is applied in the context of the risks and the products available.
There are various means by which an intermediary can make D&N part of its business processes and enable cross selling of other products. The intermediary therefore needs to consider: -
• the means by which information is gathered
o by way of application forms,
o checklist and/or
o verbal enquiry,
• and how that may differ between customers.
Categorisation
The intermediary's analysis of its market and client type is likely to be necessary to categorise customers and ascertain whether a particular form should be used for a particular customer type e.g. an individual or commercial customer, commercial or domestic property
Additionally, the intermediary's request for information must be tailored to each product type to ensure that it covers specific aspects pertinent to that product. Having undertaken a preliminary enquiry about the customer and general requirements and using an application form, setting out the information required, enables completion of proposal forms as well as compliance with obligations arising under the general duty to disclose. It may be appropriate for the customer to consider the information the intermediary has collated and whether pertinent information has been included and that it is accurate. However, also be wary of attempts by insurers to keep the general duty of disclosure by general statements in the proposal form that the assured is obliged to disclose all material facts and also of the effect of the basis clauses.
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Record keeping
An intermediary should make a record of its discussions and —if the circumstances require it - the reason for the need to give an oral advice rather than providing a statement to the customer. A proper record of advice is also for the intermediary's own protection. This should also be the case where there is a personal recommendation.
Form of documentation
On the basis that the D&N statement or any document by which collated information is recorded is provided to a customer (but particularly a lay person) for their consideration, both the layout of the document as well as the content are important. In order to avoid the customer stating that there was a misunderstanding, it must:
o be easy to read as well as being easy to understand;
• be non technical;
• use clear language and concise.
The document must be relevant to the particular customer. If the document is confusing then there is a risk that the document does not make a recommendation or inform the customer properly.
Templates for particular classes of insurance assist the intermediary obtaining and providing information to customers. If an intermediary uses

templates then it should take care to ensure that they are adequately and regularly updated, properly reflecting say the analysis of the market in respect of the relevant contract of insurance. Blindly attaching standard documents potentially may result in claims.

Context and relevance

Policies need to be considered in the context of the client's activities and needs as well as the obligations imposed upon the client in the policy wording. The client must be able to know of and be able to comply with the terms and obligations.

In the context of a business or a domestic risk the intermediary may have to consider with the customer whether any developments may occur or changes are contemplated and whether it is possible therefore for a customer's requirements to change. That in turn may result in the need for a different type of policy or different terms. For example, there may be a need to increase limits of cover or changes of geographic coverage.

Additionally, the intermediary may have to consider whether the product needs to be, or is already, flexible. Can it be amended during currency to reflect changes of risk and cover requirements?

Cover compared with demands and needs

The proposer's D&Ns should be compared with the coverage afforded under the policy to ensure that these are met.

Wordings change and are adapted, and care needs to be taken to ensure that the relevant policy for each year fits the customer for its current circumstances. In so far as the

intermediary is obliged to draw important aspects of a policy to the customer's attention e.g. warranties, then the D&Ns statement acts as a useful tool.

Practical consequences of gathering information

It is important that the intermediary knows the need for accuracy in any proposal form both because of issues relating to warranties, materiality or misrepresentation and that the customer may be asked to warrant the truth of the proposal.

Equally if the disclosure and attestation in the proposal form may be the basis of the contract of insurance , the D&Ns statement can assist in highlighting that to the customer. But, it is unlikely that a customer will understand the effect of that clause unless it is fully explained to that person and that it is explained before the cover incepts, and ideally earlier in the broking process, such that the customer is thinking as early as possible about the answers given and the overall "truth" of the proposal.

Recommendations

If there is a personal recommendation for a particular contract/policy, then there should be an explanation of suitability in the context of the demands and needs of that customer. It is important also that the intermediary highlights what demands and needs would not be by the contract. There will be a number of considerations for different classes of business but generally, there will be particular areas in the contract which the intermediary ought to give some consideration in light of the demands and needs. These include:

Insuring Clause;

o Exclusions from cover;

o Conditions of cover;

• Conditions precedent to cover;
o Claims notification provisions;
o Warranties.
The details in the Schedule to the policy should also be carefully considered and may include, for example:
o Identity of the policyholder;
o Other parties that may have an insurable interest;
o Address/es;
o Jurisdiction;
o Territorial Limits;
o Sum/s insured;
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o Excess/es;
• Special clauses and endorsements;
o Period of policy.
There may be aspects of a policy that mean the intermediary is more likely to recommend one policy over another policy and the intermediary might consider including reference to that in the statement. These may consist of a number of variables including price and security/rating of the insurer.
Caveats and qualifications - a useful tool for the intermediary
There may be occasions where a customer wishes to proceed with a particular course of action notwithstanding a recommendation from the intermediary to the contrary.
It is on these occasions that the D&Ns statement can serve as a tool if the customer has made express statements about the level of cover required or has refused to provide documents or information or indeed expressly stated that it does not want areas reviewed, then the intermediary may consider commenting on that in the statement. There may be circumstances where a recommendation may have to be caveated appropriately; a statement that the contract may not be suitable and the customer seeks to act against advice might be inserted into the statement. Should there subsequently be problems with the insurance that relate to those aspects, then the intermediary may find such record a useful point of reference.
This may be appropriate, for example, if the customer:
• has not discussed other areas of its business with the intermediary;
o has not provided copies of current policies;
o restricted the enquiry;
o refused or not co-operated with the disclosure of information.
Specific Requirements of the FSA Rules
D&Ns requirements are contained within Section 5 of ICOBS “Identifying Client Needs and Advising” — this is an indication of the two things an intermediary is expected to do.

Section 5.1 headed “General” section confirms:
5.1.1. (1) In line with Principle 6, a firm should take reasonable steps to ensure that a customer only buys a policy under which he is eligible to claim benefits.
(2) If, at any time while arranging a policy, a firm finds that parts of the cover apply, but others do not, it should inform the customer so he can take an informed decision on whether to buy the policy.
And, specifically with regard to the Disclosure of Material Facts:
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5.1.4. A firm should bear in mind the restriction on rejecting claims for nondisclosure (ICOBS 8.1.1R (3)). Ways of ensuring a customer knows what he must disclose include:
(1) explaining the duty to disclose all circumstances material to a policy, what needs to be disclosed, and the consequences of any failure to make such a disclosure; or
(2) ensuring that the customer is asked clear questions about any matter material to the insurance undertaking.
So, one can deduce from that that whatever is required by Demands and Needs, it is a requirement in addition to explaining to a customer its duty of disclosure.
What does ICOBs 5.2 require?
5.2.1 This section applies to:
(1) an insurance intermediary in relation to any policy (other than a connected travel insurance contract); and
(2) an insurer when it has given a personal recommendation to a consumer on a payment protection contract or a pure protection contract.
The rules have wide application to all types of insurance intermediary that are subjects of ICOBs (so not those dealing solely with reinsurance or large risks outside the EEA) and y policy (other than a connected travel insurance contract).
5.2.2 (1) Prior to the conclusion of a contract, a firm must specify, in particular on the basis of information provided by the customer, the demands and the needs of that customer as well as the underlying reasons for any advice given to the customer on that policy.
(2) The details must be modulated according to the complexity of the policy proposed.
This reflects Article 12(3) of the Directive 2002/92/EC of the European Parliament23, which was formulated to ensure the freedom of insurance intermediaries to set up and operate across the European Union. Article 12(3) provides:
“Prior to the conclusion of any specific contract, the insurance intermediary shall at least specj5’, in particular on the basis of information provided by the customer, the demands and the needs of that customer as well as the underlying reasons for any advice given to the customer on a given insurance product. These details shall be modulated according to the complexity of the insurance contract being proposed”.
5.2.3 provides
(1) A statement of demands and needs must be communicated:
23 See http://eur-lex.europa.eulLexUriServ/LexUriServ.do?uri=OJ:L:2003:009:0003:OO1 O:EN:PDF.
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(a) on paper or on any other durable medium available and accessible to the customer;
(b) in a clear and accurate manner, comprehensible to the customer; and
(c) in an official language of the State of the commitment or in any other language agreed by the parties.
(2) The information may be provided orally where the customer requests it, or where immediate cover is necessary.
(3) In the case of telephone selling, the information may be given in accordance with the distance marketing disclosure rules (see ICOBS 3.1.14 R).
(4) If the information is provided orally, it must be provided to the customer in accordance with (1) immediately after the conclusion of the contract of insurance.
This is similar to the requirements of the European Directive.
Lastly 5.2.3 provides:
The format of a statement of demands and needs is flexible. Examples of approaches that may be appropriate where a personal recommendation has not been given include:
(1) providing a demands and needs statement as part of an application form, so that the demands and needs statement is made dependent upon the customer providing personal information on the application form. For instance, the application form might include a statement along the lines of: "If you answer 'yes' to questions a, b and c your demands and needs are those of a pet owner who wishes and needs to ensure that the veterinary needs of your pet are met now and in the future";
(2) producing a demands and needs statement in product documentation that will be appropriate for anyone wishing to buy the product. For example, "This product meets the demands and needs of those who wish to ensure that the veterinary needs of their pet are met now and in the future";
(3) giving a customer a record of all his demands and needs that have been discussed; and
(4) providing a key features document.
Each of these components needs to be part of the intermediary's process. The FSA's viewpoint is that failure to implement them will not only be a breach of the rules but also a failing in the adequacy of the systems and controls and steps taken to ensure that the broker can be demonstrate the suitability of its advice. This is also a matter of risk management systems over the business (a breach of Principle 3). It is also likely that the FSA may conclude that the
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intermediary has failed to take reasonable care to ensure the suitability of its advice to its customers and so will be in breach of Principle 9.
o Key components of D&N
The individual requirements of ICOBs 5.2 make clear that:
o D&N must be considered before the contract is concluded; there needs to be an active process prior to inception and that process must involve the customer.
o Information must be provided by the customer; this is not a passive process for the broker. In order to consider the demands and needs, sufficient

information must be elicited, with fact finds to demonstrate the suitability of any recommendation.
o The intermediary must specify the demands and needs of the customer based, in particular, on that information provided; this requires an active process in considering the information in the context of the policy coverage available. It therefore warrants an assessment of the customer's requirements and assessment of the market.
o In the event, that any advice is given by the intermediary about the policy, the intermediary must specify the underlying reasons for that advice. This goes further than simple information gathering. It goes to reasons as to the suitability of the advice.
o The intermediary must consider the relatively complexity of the policy proposed in order to assess whether the detail given is appropriate. The main consideration for the broker is whether policies of the type requested/sought by the customer vary in extent of the coverage available. For example, are the key provisions standard in the market and are the variables ascertainable.
o Is an Assessment required in order to make a valid D&N Statement?
Yes — some form of assessment is required. As a bare minimum, an intermediary has to consider what the demands and needs of a customer are, what information has been provided by the customer and whether the policy in question matches the customer's requirements.
o What is involved in carrying out an Assessment?
The constituent elements suggest that the only way to carry out the assessment is by taking detailed information from the customer orally, analysing what has been provided, assessing it against the policy or policy that might be on offer and considering which is the best for the customer (and why) and advising accordingly. That could potentially be a time consuming and expensive process if done for each and every customer and for each and every policy. However, the broker's duties under common law or statute may require this.
Examples given in ICOBS 5.2.3 indicate the flexible nature of the task and show that the process can be very much more streamlined. In the pet insurance example given, it seems that the FSA are happy for an intermediary to put together a proposal/application form which specifies that "If you answer 'yes' to questions a, b and c your demands and needs are those of a pet owner who wishes and needs to ensure that the veterinary needs of your pet are met now and in the future." In doing so, an assumption is made that all pet owners who answer 'yes' to questions a, b and c are the same and have the same demands and needs. That may not in fact be the case. There is also the issue of what happens if the person answers 'yes' to questions a and b, but 'no' to question c. What does the intermediary do then? The FSA example statement does not provide for that. It may be that the policy being offered is still appropriate for that customer even though it answered 'no' to question c, but it is difficult to see how the intermediary can have validly complied with his/her Demands and Needs obligations if the particular response from the customer does not tally with the presumption and blanket response approach the example suggests.
The second example states that the intermediary may produce a demands and needs statement in product documentation that will be appropriate for anyone wishing to buy the product. For example, "This product meets the demands and needs of those who wish to ensure that the veterinary needs of their pet are met now and in the future." But query whether that sits with the requirement in 5.2.2 to prepare the statement "in particular on the basis of information provided by the customer" In that case the individual customer has not provided the intermediary with any information. The same might be said of the option to simply send a 'Key features document'. Again, that does not necessarily involve the customer having provided any information about his/her demands and needs.

Common law considerations

Since an intermediary will be judged according to the standard of both the FSA and the reasonable skill and care expected at common law, the intermediary cannot simply take comfort that it has complied with FSA requirements or examples.

As we have stated, under the common law, the insurance broker will not ordinarily be liable for failing to advise on the kinds of insurance a client should have: See o'Brien v Hughes-Gibb & Co Ltd24. There the broker was asked to obtain insurance for 'mortality' of a racehorse but gave no advice on other insurance products that might be available for horses e.g. against theft, when instructed to effect the mortality cover. Query under the FSA regime, whether this is a demand or a need?

If however the broker is retained to investigate the client's business or activities then there can be an assumption of responsibility to do so at common law. This will arguably go to both points

— what are the client's demands and expectations

— what the client says it requires, balanced against what in fact are the needs in relation to the enquiry

— what is it the client does not know and what is not on its "wish-list" but which are an (essential) element of the business?

24 [1995] LRLR 90

The problem is that the broker has (or may have) a generic understanding of what the customer/assured seeking insurance would require. That in turn gives rise to assumptions by the broker. The approach of the court, however, when considering such matters will be what is the reasonable expectation of the customer: first as to what the broker will do and advise upon; and second, the insurance available in light of the customer's requirements (which may be what it demands and needs).

Therefore the demands and needs regime appears potentially to be narrower than the common law requirements because the broker is arguably being required to ascertain more about the client and may be required to comment on whether the product itself meets the customer's requirements. Equally, if a client wishes to use an intermediary because of his particular expertise in placing a type of insurance, the common law may impose a higher standard on the intermediary than just making a few assumptions about the client's demands and needs and then producing a statement indicating that these presumed needs have been met.

But is "demands and needs" a general enquiry or is it restricted to those aspects upon which the broker has been instructed to advise? E.g. a customer wishes to obtain car insurance, is the broker obliged to ascertain what other insurance is required? — probably not, but if the customer does ask for a wider consultationlreview, then the broker has opened itself up to undertake a wider demands and needs analysis. By doing so, the broker has widened the potential extent of the retainer and also may be entering into areas that are beyond its ability. This begs the question — does the broker have the requisite skills to understand the nature of the client's business and assess the risks that should be insured against. If not, the broker should not be offering this service.

The solution appears to be to refine the retainer: make it clear in the retainer what it is that the parties have agreed will be undertaken. The broker needs to be sure as to the level of expertise, the capture of information and analysis and skill set to ensure that the requisite standards can be met.

This does not abrogate the general duty of a broker to make enquiry and obtain information. There may be information which ought to be disclosed, which the client has not thought it important to mention for himself. See Court of Appeal decision in McNealy v The Pennine Insurance Co Ltd25. A part-time musician did not appreciate the significance of his part-time musician status and did not communicate the fact to the broker. The Court of Appeal held that the broker should have obtained that information.

It also has to be borne in mind that under ICOBS 5.1.4 a firm has to bear in mind the restriction on rejecting claims for non-disclosure (ICOBS 8.1.1 R (3)). And ensure that a customer knows what he or she has a duty to disclose all material information to the insurer and the consequences of any failure to make such disclosure. It is difficult to see how an intermediary can comply with this aspect if the extent of its information gathering is the simplistic presumptions-based-on answers-to-limited-questions that the ICOBS 5.2.3 approach suggests. It is questionable how a broker may be satisfied that the insured is aware of/has complied with its duty of disclosure if the broker has not asked it any questions/sought any information.

25 [1978] 2 Lloyd's Reports 18

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See: Sharp and Roarer Ltd v Sphere Drake Insurance Plc26 — the judge commented a general broker effecting yacht insurance should "advise on all matters on which a lay client would in the ordinary course of events predictably need advice, in particular in the course of the selection of the cover and the completion of the proposal".

However, there are limits on an intermediary's obligation to make enquiries. A broker will not be found negligent for seeking answers to questions that he had no reason to ask. See: Dallinga v Sun Alliance Insurance Co.27 The Court held that the broker had no reason to believe goods were not the assured's property under a contents cover.

Equally, if a broker does ask appropriate questions and the insured withholds information then the broker will not be held responsible for any resulting gap in cover.

Documenting the Assessment / D&N Statement

The Rules set out in detail that the Statement must be on paper or some other durable medium (compact disk, CD-Rom), in the language of the State (English therefore in most cases), unless the parties agree another language.

The Rules provide that the Statement may be given orally where the client agrees or where urgency requires it. But there is a requirement to follow up what has been said in writing.

Regardless of Demands and Needs obligations, it is good practice for the intermediary to make notes and follow advice up in writing (by letter or email). In addition, a broker has to ensure that it records the presentation of the risk to the insurer and so these two documentary sources should be consistent: each evidencing steps taken by the broker. The FSA requires that the intermediary demonstrates the suitability of recommendations and that the customer was in a position to make an informed decision.

o The consequences of not carrying out an adequate assessment

On the face of it, an intermediary is unlikely to be sued purely for not having done an assessment or failing to produce a Demands and Needs Statement. It will however be a regulatory breach for which the intermediary may be fined. The risk to customers is that they will not receive suitable advice.

A customer/client will usually not have suffered any loss as a result of the noncompliance. However, where it does suffer a loss for some other reason, for example, an insurer has denied a claim for non-disclosure, or the client has discovered that the insurance purchased does not cover the particular damage it has sustained, it is likely that the claimant or claimant's advisors will look closely at the Demands and Needs process. If D&N was not performed properly, then this likely will be used against the broker. It may be said that the broker has not complied with its professional obligations or standards, and the lack of a proper Demands and Needs process is further evidence that the intermediary must have

26 [1992] 2 Lloyd's Reports 501

27 (1993) 10 A1taLR (3d) 59

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been negligent/has breached the terms of its contract.

Conversely, since the obligations of Demands and Needs are so closely wrapped up with the common law duties to enquire about a client's needs and to provide appropriate advice, if an intermediary has completed a proper Demands and Needs assessment and is able to document that fact, it will likely help in the defence of any claim for negligence/breach of contract. It tends to suggest that an intermediary is aware of his common law obligations and was striving to comply with them.

So it is a risk management tool (provided of course that the appropriate framework and training is in place across the intermediary's business not just on completing forms, but understanding why they are necessary in recording information, requirement and assessing expectation).

Is D&N purely an additional cost or can it add value?

Aside from the risk management aspect Demands and Needs is an opportunity to differentiate the services a broker provides from those of its competitor. Taking an opportunity to meet/talk with a client and spend time finding out what his/her demands and needs actually are (rather than what you believe or assume they might be) may assist in selling other forms of insurance that he/she were previously unaware of or had not considered.

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"EnvironCom"

Nicholas G Jones - and - (1) EnvironCom Limited (2) EnvironCom England Limited - and MS Plc t/a Miles Smith Insurance Brokers

"The rationale for the imposition of these duties on a broker is that it is an unusual obligation for a contracting party, and an area of the law which can have harsh consequences, not least because any non-disclosure relied upon by the underwriter to avoid the policy may have no causative significance as regards the claim that will as a result not be paid."

SteeleJ

This quote emphasises the stance of the Court when considering complaints against brokers in respect of the duty of disclosure.

This High Court decision addresses the duties of the broker in the context of a set of facts where a broker might ordinarily think that all that could have been done was done for the purpose of advising the client about the insurance and the duties the client has in relation to disclosure of material facts. The Court's decision examines the broker's duties and the points at which steps might be taken. What is interesting about this case is not only the steps that the broker took, but also other steps that were taken by the assured and the insurer as regards the risk that was to be insured.

The case was a negligence claim by a client assured EnvironCom against its insurance broker, Miles Smith. It followed EnvironCom' s failure to make a recovery in full against its insurer (Woodbrook) which had denied indemnity in respect of a loss due to a fire at the insured's factory premises on 16 September 2007 which destroyed its £2.1 million recycling site. The basis for the denial of coverage was non-disclosure of material facts relating to the risk. On 30 November 2007 Woodbrook elected to avoid the policy on the grounds of material non-disclosure relating to the use of high temperature plasma cutters in the process of de-manufacturing fridges and the occurrence of further fires in addition to two previous claims.
The claim against the broker was for some £6 million, EnvironCom having managed to obtain a payment from the insurer during the course of the proceedings for a costs inclusive settlement of £950,000. EnvironCom's complaint was that its broker had not advised EnvironCom, in clear and specific terms, that fires, however minor, were discloseable, and also the broker had not asked EnvironCom at the time of the final renewal preparations, whether any, or further, fires had occurred on site. The further general allegation was that the broker had not disclosed all the relevant details, including the use of high temperature plasma cutters, to the insurance provider and that had caused its policy to be voided.
The avoidance was also in circumstances where there had been a proposal form and a basis clause in the proposal form making the truth of the proposal (the facts set out in the proposal form and answers given by the assured) as the basis of the contract, and therefore making them fundamental terms of the contract whereby a misstatement was also a misrepresentation and non-disclosure to the insurer. Basis clauses have been much criticised but they still arise and place a high onus on the assured (and therefore on its broker to explain the effect of the clause).
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The terms of the basis clause were:
"To the best of my knowledge and belief the information provided in connection with this proposal, whether in my own hand or not, is true and I have not withheld any material facts. I understand that non-disclosure or misrepresentation of a material fact will entitle the Underwriters to void the insurance.
(NB. A material fact is one likely to influence acceptance or assessment of this proposal by Underwriters; if you are in any doubt as to what constitutes a material factyou should consult your Insurance Advisor.)"
This declaration went on to say:
"I understand that signing this proposal form does not bind me to complete the insurance but agree that, should a contract of insurance be concluded, this form and the statements made therein shall form the basis of the contract. ".
In defence of the claim Miles Smith relied primarily on the documents they sent out to
EnvironCom as containing adequate education to the client on the obligation of disclosure.
These included a document giving a summary of the assured's obligations.
The Court concluded that the documents that the broker had sent to EnvironCom were inadequate to satisfy the broker's duty of explaining the obligation of disclosure to EnvironCom. In addition, where an inappropriate and incomplete explanation was afforded to a client as to its obligations, there was a higher standard of care required on the part of the broker in eliciting material information for disclosure.
The Facts
EnvironCom' s business is a specialist business of dismantling and recycling of white goods that contain CFCs and in particular freezers. EnvironCom

has “a state of the art 10 acre site” on the outskirts of Grantham, in Lincoinshire. It had installed capacity to receive, treat and process a vast range Waste Electrical & Electronic Equipment (WEEE). The facility dealt with the treatment of various products including fridges and freezers, flat Screens, IT Equipment aimed at achieving high levels of WEEE Recycling, Recovery and Reuse.

Miles Smith acted as insurance broker for the claimant EnvironCom putting in place various insurance polices for EnvironCom including commercial combined insurance covering property and business interruption risks with Woodbrook for a period of over 3 years (between 2004 and 2007) including May 2007 to May 2008 being the relevant policy year of claim. In that time Miles Smith visited EnvironCom’s premises and also there were various surveys conducted of the premises and the business processes undertaken by EnvironCom, either at the request of the insurers, or at the request of Miles Smith on behalf of EnvironCom. Some of the reports for the insurers contained recommendations and requirements, and these latter elements of the reports on occasion were provided to EnvironCom for them to address and implement changes, whilst other aspects of the report were retained by the insurer for its sole use. In addition, during the three year period in which Woodbrook provided insurance, there were various fires at the assured’s premises, some of which were disclosed to the insurer, some of which were investigated by the insurer (using its own fire investigation specialists), and some were investigated by EnvironCom’ s own investigators. Despite these the broker obtained an insurance policy liaising with

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EnvironCom.

EnvironCom’s process of dismantling white goods that contain CFCs and in particular fridges and freezers was to ensure that CFCs either in liquid form or in the materials used in the construction of the goods were trapped and contained such that they would not leak into the atmosphere. (CFC5 having been identified as adding to global warming and the consequent need for manufacturers to ensure that freezers may be recycled and the CFCs existing in compressors and the foam in freezers by law have to be properly dealt with to conform with the relevant legislation).

The process to be used was quite sophisticated and it involved the trapping of the cooled gases in the freezer unit and then crimping the piping to the container that contained the CFCs. The parts of the freezer were then recycled with metal and polystyrene foam being shredded and separated and thereafter. Material was to be shredded into different sizes depending upon the shredding process, and then foam recycled into blocks, whilst the metal also was recycled. The bricketing of the foam, as it is called, also involved the use of heat to mould the foam. The foam itself existed in different forms and some was more inflammable than others. Although some may not have contained CFCs, there was a risk in the process of combustion as heat was generated.

One aspect of the recycling process involved the removal of bolts which, if they could not be removed easily, required the use of a plasma gun or cutter to apply extremely high heat in a concentrated area which enabled bolt removal, cutting through the metal. This gave rise to a risk of combustion since the hot metal or sparks from the cutter might ignite the insulation. The bolt removal was relatively early on in the process and thereafter the refrigerators would be de-gassed, and shredded. The Judge described the use of high temperature plasma cutters to recycle highly flammable pentane fridges a “potent mix”.

See: the sequence of events (Appendix 1).

In 2004, discussions took place between EnvironCom and Miles Smith about property and machinery breakdown insurance as the construction of the

fridge recycling plant neared completion. The broker recorded detail about the recycling plant and machinery and was sent further detail on request about the equipment and the recycling process and that was provided to insurers.

In May 2004 Woodbrook provided cover subject to a completed proposal form and a satisfactory survey of the property and operations then started in June 2004. The proposal form (with basis clause) was completed and signed and did not request detailed information about the process used; The insurer's survey report was not disclosed to Miles Smith or EnvironCom. Although it described the process, it did not describe the method or tools used. Although it observed the use of heat, it did not consider it overall a hazard in the process. Risk improvements were made on insurers' request and this was addressed in an endorsement to the policy.

When providing the combined policy documents, Miles Smith stated to EnvironCom:

.please ensure the cover is adequate for your requirements and try to familiarise yourself with the terms and conditions... You are duty bound to notz)5' us of any material changes that may affect your cover and advise of any alteration and/or claims as and when they arise."

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During the relevant period EnvironCom's personnel with responsibility for insurance changed. EnvironCom's new insurance manager requested a summary of the existing cover which was given and Miles Smith informed EnvironCom that specific warranties had to be complied with and also of a continuing obligation to notify Insurers of any "Material alterations to risk", giving examples of "Change in business activities/acquisitions or disposals"; additional premises/Risks/Insurable Items or onerous Contract Conditions. It also highlighted that answers or statements in a proposal form or otherwise would be EnvironCom' s responsibility and that:

"if incorrect information is supplied it could result in the Policy being repudiated on the basis of non-disclosure or misrepresentation ".

The document stated that changes in information or material facts should be notified to Miles Smith. Subsequently in January 2005, Miles Smith forwarded a new TOBA to EnvironCom which stated:-

"Utmost good faith and duty of disclosure

The law imposes onerous duties upon anyone entering into an insurance contract and anyone acting on his behalf A proposer has a duty to disclose all facts that may influence the insurer in deciding whether to accept insurance, impose special terms or charge an increased premium. This duly arises not only at inception of the contract but also applies to the submission and substantiation of all claims.

A proposal or claim form or any other document relating to the contract of insurance must be answered fully and accurately, the provision of such information/documentation being the sole responsibility of the insured."

This was signed by EnvironCom.

Miles Smith made further visits to EnvironCom's premises and ran through a list of potential insurance needs for EnvironCom and subsequently there was renewal of the Combined policy and a further insurer report compiled. There were then series of small fires in various shredders. These were investigated and various reports were compiled for the insurer and for EnvironCom, but no action taken although specialist advice was recommended.

In May 2006, the insurer offered renewal terms (again subject to survey) which were accepted. The renewal document also stated that the assured should advise insurers of:-

"any circumstances which could alter their assessment of the risk."

Insurer's further survey report highlighted a "high inception hazard" and "the potential for a rapid and short fire spread"
The broker's staff then changed in 2006. There were then some further fires. Insurers renewed in May 2007, having first stated that they would not offer terms. Subsequent further fires followed culminating in the loss in November 2007.
According to evidence, plasma cutters were mentioned just twice when Woodbrook were EnvironCom's insurers; once in a telephone notification to Miles Smith of a theft of the equipment, which was not pursued; and again when they were identified as a possible source

of ignition in the fire risk assessment in October 2006. But that assessment was never sent to Miles Smith.
Other facts:
- The Insured had not disclosed other fires;
- Breaches of waste management licence;
- Enquiry about fires would have revealed the use of plasma guns.
Judgment
The claim was dismissed because Miles Smith's failures were not causative of the loss, but the Judge stated in relation to disclosure that:- "The broker must sati.ft 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 on ginal placement and at renewal..."
Dealing with the scope of a broker's duty in placing or renewing insurance cover for a client, the Judge referred to the FSA Insurance Conduct of Business Handbook dated May 2007 and in particular Rule 4.3.1 and 4.3.2. [The FSA Rules changed in 2008, but the thrust is broadly similar. See appendix 3]. The Judge summarised the duty of a broker:
a) must advise his client of the duty to disclose all material circumstances;
b) must explain the consequences of failing to do so;
c) must indicate the sort of matters which ought to be disclosed as being material (or at least arguably material);
d) must take reasonable care to elicit matters which ought to be disclosed but which the client might not think it necessary to mention.
In the Judge's view, the foregoing flowed from the requirement that the broker should take reasonable steps to ensure that the proposed policy is suitable for the client's needs. By definition, a policy which is voidable for non-disclosure is not suitable.
The Judge considered that a broker must ensure that an appropriate understanding of questions of materiality is held by the person in the client and any new person in the client dealing with insurance. The client needs to be advised to err on the side of caution so as to disclose anything that might impinge on the judgment of a competent underwriter in assessing the risk and be helped to unearth such matters.
The Judge concluded that the broker's information afforded little or no help to the client/customer on understanding the obligations to disclose material facts, the nature of material facts or the consequences of failing to disclose them, nor did they assist in stating at what stage disclosure was required, what might be material or any warning as to the consequences of any failure to disclose.

Although the invoices for premium sent by Miles Smith from time to time gave notice of the obligation to disclose circumstances (which could alter the underwriter's assessment of the risk, and the consequence of failure to do so), again there was no explanation of what would be material. In any event the invoices were furnished after the relevant policy incepted, such that disclosure did not appear to be a post contractual obligation.
The Judge considered there was confused and incomplete written material and no adequate explanation was given of the obligation of disclosure. He considered that a written standard form explanation was not sufficient and to satisfy himself the broker must have specific oral or written exchange on the topic, both at the time of the original placement and at renewal (particularly if a new person has become that client's representative).
The Judge however was unable to accept the proposition that Miles Smith had a duty to inquire about the use of Plasma cutters even though they may have been shown them. The Judge considered that the brokers had no technical expertise in the field of fridge recycling and so could not be expected to comprehend more than the general industrial process involved. It remained the client's task to identi)5' detailed processes.
The Judge found on the facts that enquiries by Miles Smith about heat sources or "hazardous processes" would not have yielded a reference to the plasma cutters and concluded that EnvironCom would have not considered them material. In conclusion -
a) Miles Smith failed to give adequate advice to EnvironCom as to their disclosure obligations.
b) Miles Smith failed to take adequate steps to elicit information requiring disclosure.
c) If Miles Smith had complied with their obligations: i
the use as such of plasma cutters as a part of the recycling process would probably have remained undisclosed. The Judge concluded that EnvironCom did not regard the use of plasma cutters as intrinsically hazardous or even as enhancing the risk of claim on the policy and therefore EnvironCom would still not have recognised their use as material.
ii) but the existence of regular small fires (and their association with the use of plasma cutters) and the fire on the 14 March 2007 would probably have been disclosed.
The Judge considered that the broker's TOBA did outline in broad terms the obligation of disclosure, but the document did not help in determining at what stage disclosure was required, what might be material or any warning as to the consequences of any failure to disclose. Using invoices to advise about the obligation to disclose circumstances which could alter the underwriter's assessment of the risk were not of great use after the relevant policy incepted.
There was agreed expert evidence that:
- An insurance broker was under a duty to satisfy itself that its client understood the obligation of disclosure to insurers; and
- Specific oral or written exchange on the subject at the time of placement; and there
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should be at the time of renewal;
The broker's duty includes eliciting material information for disclosure.
The broker's duty did not extend to asking detailed questions about specialised processes or the specific tools used.
In light of the other facts which had not been disclosed, such as the fires and breaches of license, the Judge concluded that "even if cover was obtained despite the additional disclosure..., the resulting policy was at its lowest highly vulnerable to avoidance for further non-disclosure."

EnvironCom's chance of obtaining cover was purely speculative. The prospect of EnvironCom accepting revised insurance terms as might have been offered was remote.

Analysis

Although what the broker did or did not do was not found to be causative of the loss, it highlights the duties that the broker has when dealing in respect of demands and needs and the extent of the obligation to carry out demands and needs.

Decision points

There had been various instances when the broker may have discussed the issue of disclosure with the client, and if done so at the relevant time then the material facts may have been ascertained. These instances were:

o The start in February 2004 when the initial discussions took place;

o Each tour of the plant in 2004 and 2005;

o When communications were sent about the process and the plant;

a November 2004 and renewal of the liability policy. The explanation of matters could have been expanded;

a The TOBA in January 2005 and a wider explanation of the duty of disclosure;

a Each of the 2005, 2006 and 2007 renewals of policy.

Implications

The judgment underlines the duties that the broker has when dealing in respect of demands and needs and the extent of the obligation to carry out demands and needs assessments, but also that satisfaction of that in itself does not satisfy the overall duties that the broker owes to a client assured. Further, it highlights that particular matters must be discussed with and highlighted to the client assured not only at the initial stages of the retainer, but also should be considered by the broker throughout the retainer, and if necessary for them to covered again by the broker if the circumstances require, and to be alive to the on-going duties. The broker must ensure that the assured understands the need for complete disclosure, in effect needing to review what has gone before in previous years, rather than simply building on

changes since the previous policy year. The impact of changes generally, but in particular with regard to those persons involved with the relationship between the broker and the client/assured, must be considered carefully. Relying on documents and guidance sent to the company in previous years will not satisfy the requirement.

EnvironCom demonstrates the standards of care and professionalism by which a Court will judge the broker's performance are founded upon the common law benchmarks of duty of care as applied to any other professional person.

Generalised, written standard form explanations/written warnings about the duty of disclosure are not sufficient. The client has to have a full understanding of the duty. A broker should not make broad assumptions about an insured's understanding of the proposal and renewal processes. There may be instances where the client appears a relatively sophisticated buyer of insurance, but even in those circumstances, the broker needs to consider covering aspects and ground that may seem fundamental or obvious. This may entail verbal or written exchanges on the subject. A risk manager at the assured must fully understand the nature and scope of the duty of disclosure.

It underlines that it is all the more important that the lay client is told of the paramount duty to disclose and what it involves. A client needs to be advised as to what is material. A broker cannot expect to satisfy its duties by relying on generic advice for clients and provide examples to clients that may not be appropriate or useful, since it is not possible to think of all the different circumstances where the client may have material information. Extensive enquiry is required by the broker and a broker's detailed understanding of the coverage of the policy should enable the broker to consider whether the client should give specific consideration to a particular aspect, in the context of the duty of disclosure.
A particular process that has high risk elements in particular stages (as seen from the standpoint of an ordinary individual) may not seem material to an assured. However the broker is not obliged to have in-depth technical knowledge.
In this case though the focus was on material "alterations" to risk such as "additional premises". The client was told to told that if there was "any fact which may affect underwriter's attitudes you should make it know (sic), whether it is specifically requested in the Proposal Form or not".
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Appendix 1
Daryl Fisk v Brian Thornhill & Son (A Firm) [2007] EWCA Civ 152
This ruling of the Court of Appeal followed a six year legal battle surrounding the flooding of The Sun Inn in Essex. Daryl Fisk was the producing broker instructed by the publicans to arrange property insurance for their establishment. The placing broker, Brian Thornhill, provided a quotation expressly on the assumption that the Inn was of standard construction, being either brick or stone, with a slate or tile roof ("BSST"). In the proposal form, it was stated that the building was constructed of lath, plaster and timber. The query as regards roofing materials was left unanswered.
One year later, the insurance was due for renewal. As placing broker, Brian Thornhill provided Mr Fisk with a renewal notice. In fact, this was not a renewal as Brian Thornhill was placing cover with a different insurer. This was not known by Mr Fisk or the Assured. Mr Fisk instructed Brian Thomhill to renew on quoted terms, and Brian Thornhill subsequently requested a quotation, which included a warranty that the building was BSST. A copy of the quotation was not supplied to Mr Fisk or the Assured. Acceptance of cover was conditional upon the proposal form being submitted within 30 days of inception.
On 21 October there was a flood, which damaged the Inn. Brian Thornhill did not provide Mr Fisk with a proposal form until 23 October. On 5 December, insurers refused cover on the basis that the Inn was not of standard construction.
The case brought by the Assured against the producing broker, Mr Fisk, settled. The question for the Court of Appeal was whether Mr Fisk was entitled to receive a contribution of 25% from Brian Thomhill towards the damages paid. The Court held that Brian Thomhill should not have given the warranty based on information from the previous year. They should have made further enquiries, particularly given the vagueness of the answers on the previous year's proposal form. Further, it was a breach of duty to not obtain the proposal form prior to placing cover, especially as Mr Fisk and the Assured had not been informed of (a) the insurer's terms and conditions; and (b) the consequences of correcting in the proposal a statement made in the quotation request.
Comment:
This case provides some useful guidance as to a broker's duties at renewal. The Court of Appeal emphasizes the importance of ensuring that all practicalities are taken care of prior to inception of cover. The case is a clear demonstration of the continuing need to keep an insured informed of all

changes and requirements regarding the insurance as and when they arise.
44
Chronology
February 2004
16 March 2004
25 May 2004
June 2004
1 June 2004
10 August 2004
August 2004
1 September2004
25 November 2004
Discussions between Environcom and Miles Smith about property and machinery breakdown insurance as the construction of the fridge recycling plant neared completion.
Visit on 4 February 2004 by broker. Recycling plant and machinery.
Fax sent to broker: “breakdown of plant values and details of conveyor parts and what they do”.
Cover subject to a completed proposal form and a satisfactory survey
Environcom Grantham operation starts.
Environcom completed the proposal form.
Survey for underwriters. Certain “Requirements” and “Recommendations”.
Endorsement No. 1.
Miles Smith letter to Environcom regarding “duty bound to notz)5’ us of any material changes that may affect your cover “.
Miles Smith letter to Environcom regarding impending renewal of their liability policy. “Summary of Insurance” provided focusing on the need to update the description of the business to take account of any new acquisitions or developments. Issues included:
Warranties with an explanation about invalidating the Policy Material Facts - not ij5 Insurers of any Material alterations to risk
Proposal Form and other information which will form the basis of an Insurance Contract.
Changes
Fact ... which may affect Underwriters attitudes.. whether it is specifically requested on the Proposal Form or not”
revised terms of business to Environcom (FSA authorisation). Referring to the Utmost good faith and duty of disclosure.
Appendix 2
Nicholas G Jones - and - (1) Environcom Limited (2) Environcom England Limited
- and MS Plc t/a Miles Smith Insurance Brokers

7 January 2005
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20 January 2005
27 April 2005
24 May 2005
21 June 2005
27 October 2005
February 2006
23 February 2006
March 2006
23 May2006
27 June 2006
22 September 2006
27 September 2006
4 December 2006
21 December2006
27 December 2006
22 January 2007
15 March 2007
17 April 2007
2 May 2007
Environcom signed and returned.
Miles Smith tour of premises: identified that Environcom were underinsured.
Renewal subject to survey.
Underwriter survey of plant.
Fire near Shredder II. [Burgoynes, a specialist forensic fire investigation firm final report nearly a year later dated 22 September 2006]
A surveyor from Aspen Ltd for the purposes of renewal of EnvironCom's liability cover (as instructed by broker).
Environcom notified of Aspen Ltd report.
Environcom - "Process Description" of fridge destruction process, omitting plasma gun to remove the compressor bolts.
Renewal of policy.
Further survey (not disclosed to broker or Environcom).

“high inception hazard” and “the potential for a rapid and short fire spread”.
Burgoynes final report - probable mode of outbreak of the fire was the ignition of pentane, although the source of that ignition remained unknown.
Recommended consultant report on equipment.
Peninsular report with fire risk assessment - low risk.
Broker e-mail with renewal questionnaire for liability cover.
A small fire occurred on the fridge line in part of the briquetting plant.
Serious fire in the briquetting plant (due to water damage from prior fire).
Environcom updated broker on improvements.
Smailfire in Shredder III. This was put out with a fire extinguisher.
Broker states that Underwriters wanted to know of “any additional procedures in place to prevent further losses following the two fire claims in recent years.”
Underwriters refuse renewal terms: adverse claims experience.
46
16 May 2007
22 May 2007
24 May 2007
July2007
6 September 2007
16 September 2007
Environcom improvements.
Not a case insurers would like to invite renewal.
Stringent renewal terms offered.
Insurer resurveyed. Plasma cutting equipment.
Fire.
Further fire in Shredder II: fire which destroys £2.1 million recycling site.
30 November 2007
Insurers elect to avoid policy.
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Appendix 3
FSA Insurance Conduct of Business Handbook dated May 2007
Extracts from ICOB 4.3
4.3.1 (1) An insurance intermediary must take reasonable steps to ensure that, if in the course of insurance mediation activities it makes any personal

recommendation to a customer to buy or sell a non-investment insurance contract, the personal recommendation is suitable for the customer's demands and needs at the time the personal recommendation is made.

4.3.2 In assessing the customer's demands and needs, the insurance intermediary must:

(1) seek such information about the customer's circumstances and objectives as might reasonably be expected to be relevant in enabling the insurance intermediary to identify the customer's requirements. This must include any facts that would affect the type of insurance recommended, such as any relevant existing insurance;

(2) have regard to any relevant details about the customer that are readily available and accessible to the insurance intermediary, for example, in respect of other contracts of insurance on which the insurance intermediary has provided advice or information; and

(3) explain to the customer his duty to disclose all circumstances material to the insurance and the consequences of any failure to make such a disclosure, both before the non- investment insurance contract commences and throughout the duration of the contract; and take account of the information that the customer discloses.

In relation to 4.3.2 (3), an insurance intermediary should make clear to the customer what the customer needs to disclose. For example, in relation to private medical insurance, this could include any existing medical condition where relevant, or in relation to motor insurance, any modifications carried out to the vehicle.