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An examination of the legal liabilities of insurance intermediaries and the insurance thereof.

Jowairiya Mahomedy

A dissertation submitted to the Faculty of Commerce, Law and Management of the University of Witwatersrand, Johannesburg in fulfilment of the degree of Master of Commerce (Insurance and Risk Management)

December 2010

Declaration

I hereby declare that this is my own unaided work, the substance of or any part of which has not been submitted in the past or will be submitted in the future for a degree in to any university and that the information contained herein has not been obtained during my employment or working under the aegis of any other person or organization other than this university.

---------- ----------

(Name of candidate) Signed

Signed this _____ day of _____ 2010 at the University of the Witwatersrand, Johannesburg.

Acknowledgements

1. My friends and family for their support and encouragement.
2. My supervisor, Mr. Frank Liebenberg. Not only have you been an invaluable lecturer throughout my postgraduate studies, but you have guided me, encouraged me, and most importantly believed in me when at times I did not believe in myself. I would not be where I am today had it not been for you – I am forever indebted to you.
3. Prof. R.W. Vivian for the countless hours spent guiding and helping me throughout this process. I am honoured to have had the opportunity to gain from your limitless knowledge; thank you.
4. Mr. Justus van Pletzen and the Financial Intermediaries Association of South Africa for their support.
5. My colleagues at Camargue Underwriting Managers and Phoenix Underwriting Managers (the 'Camargue Group') who have been so helpful and so willing to share their knowledge with me; and especially to Mr. Mitch Marescia.

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Abstract

The insurance product is marketed by various distribution channels, most notably that of the insurance intermediary. The extent of the intermediary's role within the insurance transaction, exposes the intermediary to liability risks; these liabilities could arise either in contract, delict or statute or be sui generis. This dissertation sets out the extent of the legal liabilities exposure of insurance intermediaries within the South African market against an international background and the insurance thereof.

Keywords: insurance intermediary, liability insurance, professional liability, insurance pricing

1. INTRODUCTION

Stettler, Eugster, and Kuhn (2005:13) define insurance as "an operation by which one party, the insured, obtains from another party, the insurer, the promise to indemnify the insured or a third person in the case of a loss. The payment of this service is called premium. The insurer accepts a totality of risks and compensates the insured or a third person according to statistical laws." Insurance is essentially the promise to indemnify the insured or a third party should a well-defined contingent event occur. Arrow (1971: 220) suggests that insurance is a type of contract with an "exchange of money now for money payable contingent on the occurrence of certain events".

The distribution of insurance occurs through a variety of channels, as noted by Kim, Mayers and Smith (1996), with many insurers marketing their insurance products directly to buyers either by mail, telemarketing, or sales representatives. However, most insurance transactions will involve an intermediary who will link the buyer of insurance and the insurer and essentially be the link between these two parties. Cummins and Doherty (2005: 5-6) define an intermediary as "an individual or business firm, with some degree of independence from the insurer, which stands between the buyer and seller of insurance".

Hoyt, Dumm, and Carson (2006) suggest that insurance is distributed either through the captive agency (also known in South Africa as tied agents) system characterized by agents who represent a single insurer, the direct response system, the broker system, or the independent agency system.

In practice the distinction between brokers and agents is not clear as both these intermediaries essentially perform many of the same tasks. Cummins and Doherty (2005: 1) note that while brokers are traditionally described as agents of the policyholder and insurance agents as agents of insurers, this separation is more a matter of emphasis than a watertight division. A distinction between agents and brokers can be made in the size of business conducted and the range of services offered; agents tend to place smaller business and provide fewer services than brokers. However agents and brokers basically perform the same function as intermediary, they both

bring together appropriate buyers and insurers; they are ‘market makers’. For the purposes of this dissertation, the term ‘intermediary’ is used to refer to both independent agents and brokers. However the main issue in determining the difference between agents and brokers lies in who has authority with respect to specific transactions; where an agent can bind the principal a broker cannot.

The principal role of the insurance intermediary is to bring together the insurer and the insured, thereby facilitating the creation of a contract between the insurer and the insured. This is the service for which the intermediary will be remunerated, in the form of a commission from the insurer; however the insurance intermediary may choose to provide additional services. Essentially the intermediary is rewarded by the insurer for bringing business to the insurer. It is possible for the intermediary also (or exclusively) to be rewarded by the insured for service provided – the fee for service model.

Most insurance products are complex goods; to choose between the diverse options and suppliers available requires some expertise in the field. The buyer of insurance is faced with a difficult decision in that the choice of product and insurer will depend on a number of factors, including the reputation of the insurance company for efficient payment of losses and the financial capability of the insurer to sustain the losses. The buyer must decide what insurance protection is needed given the risks faced and then compare policies in order to decide which is best suited for the buyers’ particular needs. The intermediary will help buyers of insurance identify their risk and coverage needs as well as match these buyers with suitable insurers.

It is precisely the intermediary’s knowledge of the insurance market and insurance services, as well as their ability to find appropriate insurers to provide price quotations that makes the use of an intermediary appealing. In this way the use of an intermediary reduces transaction costs (Eckardt; 2002). The role of the insurance intermediary is both complex and multidimensional. As noted by Cummins and Doherty (2005) an intermediary must “scan the market, match buyers and sellers with insurers who have the skill, capacity, risk appetite, and financial strength to underwrite the risk, and then help their client select from competing offers”. Eckardt (2002: 5)

notes that because of high information asymmetries and high search costs insurance intermediaries play an important role in mediating between two market sides.

Trust is also a crucial feature in the placement of insurance contracts by intermediaries as the policyholder must rely solely on the relationship between the intermediary and the insurer when placing risks; these contracts will thus be governed by the principle of 'utmost good faith' and an intermediary who does not have strong working relationships with insurers will experience difficulty in placing business.

Given the significant and complex role of the insurance intermediary in the insurance transaction, the extent of the legal liability exposure of the intermediary becomes a pertinent issue. Legal liabilities can arise either from the law of contract, the law of delict, from statute, or be *sui generis*. The law of contract governs legally enforceable agreements, the law of delict is essentially a 'civil wrong', and statute is those legislations that are passed by Parliament. *Sui generis* obligations are those which do not comfortably fit into any of the previous three categories and have been created largely by judicial decisions.

As insurance is arranged by means of an insurance contract; the rights and duties of the parties to the contract are governed by the law of contract, as applied to insurance contracts. However, insurance contracts may not only be governed by the common law, but may also be governed to a certain extent by legislation. Furthermore, liability claims arise mainly from the law of delict. Thus it would seem that the legal liabilities of the insurance intermediary could stem either from contract, delict, or statute.

If an intermediary, for example, fails to convey material information that has been supplied by the buyer of insurance to the insurer, and the insurer repudiates the claim, what should the consequences be? Or more generally, what are the legal consequences when the intermediary is negligent or at fault? And who should bear these consequences? This gives rise to another pertinent issue: when considering specific transactions, on whose behalf is the intermediary acting with respect to that transaction, the insurer or the insured?

Bennett and Malekan (2004) note that broker malpractice suits have increased substantially in recent years with policyholders looking to intermediaries as a right of recourse when they suffer a loss especially as a consequence of the repudiation of a claim by an insurer. Such claims will arise for a number of reasons including the policyholder's reliance on the intermediary for advice. The policyholder's ability to recover from the intermediary will depend on the nature of the intermediary's actions as well as the nature of his duties imposed by law. Furthermore the intermediary could be sued on his duty as a professional or his fiduciary duties.

This dissertation explores the legal liabilities of insurance intermediaries and the insurance thereof and begins with a general overview of the principles pertaining to liability, particularly the problem of concurrency of actions and liability for pure economic losses. The insurance of intermediaries is then examined, with particular reference to liability insurance and professional indemnity insurance. The roles of functions of the insurance intermediary are discussed, including the principal-agent problem, agency law and vicarious liability. This is followed by a review of case law in order to establish how the law is applied to intermediaries, both within South Africa and elsewhere. The pricing of insurance policies is also considered and increased limit factors, deductible credits, and rate on line percentages are determined for the South African professional indemnity market. This dissertation then concludes with recommendations for future research.

2. GENERAL PRINCIPLES OF LIABILITY

The basis of liability is founded in two sources and as noted by Gaius (170: 179). He noted that every obligation arises either from contract or from delict. Zimmermann (1990) notes that the modern use of the term 'obligation' refers to a two-ended relationship where, on the one hand, there is a personal right to claim, and on the other, there is a personal duty to render a performance. Since the time of Gauis two further sources of liability can be added, namely that of statute and *sui generis*.

Broadly speaking an insurance intermediary may be held liable for breach of contract, breach of tort (delict in South Africa), breach of common law duties, and fraud. In most instances the insurance intermediary will be acting on the basis of a contract; if the insurance intermediary is alleged to have breached the contract then an action will arise in contract. In certain situations liability may also arise from the negligence of the insurance intermediary and in this event an action will arise in delict. An insurance intermediary may be held concurrently liable in both contract and delict. If an intermediary is sued by a third party, then the action must be based in delict since no contractual relationship exists between the intermediary and the third party. As a professional the insurance intermediary will owe common law duties to the insured such as fiduciary duties and the duty to act with care, skill and diligence. Carciumaru (2009) notes that in South Africa, in relation to Directors, a breach of a fiduciary duty have evolved under *sui generis* whilst a breach of the duty of care is delictual in nature. The legal position of insurance intermediaries is therefore primarily governed by the general principles of law and in particular by the law of agency (Havenga; 2001: 14)

This chapter explores the theoretical bases of the relevant actions involved in litigation against an insurance intermediary. The contractual and delictual bases of liability will both be considered and the requirements of each will be discussed in terms of South African law, with specific reference to insurance intermediaries where applicable. Liability in terms of statute and *sui generis* will also be discussed. Moreover, consideration will be given to overseas jurisdictions where relevant.

2.1 Law of contract

A contract is an agreement giving rise to obligations which are enforced or recognized by law (Treitel, 1995: 1). Contractual obligations differ from other legal obligations in that they are based on the agreement of the contracting parties. Failure to observe such obligations will result in the liability to pay compensation in the form of damages. In practice, the liability of an insurance intermediary will usually lie in contract as the insurance intermediary will always have entered into a contract, especially a mandate, with the insured to perform specific obligations.

According to the law of obligations, Fridman (1976: 3) notes that the rights and duties which arise from such agreement are said to be *in personam, i.e.*, applicable to and between the particular, individual parties, as contrasted with rights and duties *in rem*, which apply to, and between all people, *e.g.*, those which arise from the law of tort. The law of contract thus involves situations in which agreements between particular people are legally binding.

Esser (1996: 604) suggests that contract law is "a body of legal principles enforcing obligations explicitly consented to by the parties to an agreement, in contrast to other bodies of law (torts, criminal law) enforcing obligations implicitly on individuals by virtue of their membership in a community or some other noncontractual source". Atiyah (1978) notes that the law of contract constitutes those obligations which are voluntarily assumed, whereas the law of tort constitutes those obligations which are imposed by law.

The American Law Institute (1981: §1) defines a contract in the Second Restatement as: a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty. Holmes (1881) notes that a promise could be said to be the common element of all contracts; contracts being dealings between people to make arrangements for the future. Goetz and Scott (1985) further suggest that a contract in law is essentially an exchange of promises between parties, the function of this promise being to provide information about future happenings.

2.1.1 Historical development of contract law

Weeramantry (1967: 3) notes that a striking feature of many legal systems is their lateness in evolving any general theory of contract. Teeven (1990) suggests that even by 1400 AD no modern theory of contract law had developed, however the groundwork had been laid. "It has long been assumed that the development of modern contract law was complete once English judges had declared late in the sixteenth century that 'a promise on a promise will maintain an action upon the case'" (Horwitz; 1974: 917); however modern contract law developed fundamentally in the nineteenth century.

As noted by both Weeramantry (1967) and Horwitz (1974) the origins of the law of contract are founded in economic and legal exchange. Teeven (1990: 1) suggests that "in circumstances where an economy is not directed by market forces and where a society delineates a person's rights based on the status one was born into [as was the case during the Middle Ages], there is little need of, nor opportunity for, either freedom of contract or a flexible contractual device for planning. In the main, these early contractual relations did not involve obligations to be performed in the future but rather concerned present exchanges of feudal obligations without any money changing hands".

The first commercial transaction to appear was bartering and thereafter, with the emergence of currency, bartering evolved into sales and loans and, with the latter, into contracts of mortgage and surety-ship. Cohen (1933: 557) notes that the changing of the old rules from the *ius civile* to the *jus gentium* and praetor's edicts in Roman contract law signify the effects of commerce on the law and further that "the expansion of the regime of contract since the seventeenth century has been intimately related to the modern commercial revolution in northern Europe following the development of trade with India and America".

However, when considering the history of contract, Holdsworth (1903: 82) suggests that while it is one thing to say that agreements and promises have existed in a remote antiquity, it is quite another to say that they were contracts in the sense that they were enforceable at law.

As the law developed there was a distinct shift of emphasis from form to intention and Weeramantry (1967: 2) notes that "this trend resulted in a steady movement of the law towards the principle that a promise by its very nature engenders an interest in its performance; and that its claim to enforceability springs not from the shape that it may take but from the fact that it was made"; this saw the extension of the scope and availability of contractual rights and remedies.

Weeramantry (1967: 6) notes that in mature Roman law Gaius (170) recognized four nominate contracts (a number of innominate contracts also existed):

1. *re* – contracts effected by delivery of a thing in one of four ways: *mutuum*, *commodatum*, *depositum*, and *pignus*,

2. *verbis* – by the stipulation,
3. *litteris* – by entry in a ledger, and
4. *consensus* – contracts recognized as arising immediately the parties signified their consent; these were contracts of sale, hire, partnership, and mandate.

However, as noted by Lee (1956), even though there was a Roman law of contracts, this barely amounted to a law of contract; that is to say there was no general theory of contract besides special classes of contract on which the law was based.

Furmston (1986: 1) notes that early English common law was mainly concerned with serious crime and land tenure and further states that "[Ranulf de] Glanvill[e] writing in about 1180, tells us that in his time, 'it is not the custom of the court of the Lord King to protect private agreements'". The field of private agreements in England evolved during the thirteenth century to be dominated by a number of writs, the most important of these writs being the Writs of Debt, Covenant, and Account.

English contract law as we know it today developed around a form of action known as the action of *assumpsit*, which came into prominence in the early sixteenth century as a remedy for the breach of informal agreements reached by word of mouth – by 'parol' (Furmston; 1986: 1). This new action of *assumpsit,* introduced in *Slade's Case*, triumphed over the old Writ of Debt and covered situations which should be regarded as contractual but for which no other action existed. The main point of *Slade's Case* was whether *assumpsit* should be available in cases already covered by another action, the action of debt, given the established rule that an action on the case would not lie if another form of action lay on the same cause of action (Ibbetson; 1984: 295). *Assumpsit* became the contractual action of the common law after *Slade's Case* and provided English law with a comprehensive remedy for breach of contract. Wilson (1993) further notes that it was out of the ruling in *Slade's Case* that the modern doctrine of contract developed.

Another significant development in the sixteenth and early seventeenth centuries, as mentioned by Furmston (1986) was the introduction of a doctrine that defined the scope of the newly recognized promissory liability. It was this extension of liability [i.e. the extension of

promissory liability into areas previously outside the scope of common law] that necessitated the rise of the doctrine of consideration as a means of distinguishing actionable from inactionable agreements; and with this formalization modern contract doctrine began to take shape (Wilson; 1993: 282).

2.1.2 General principles

"A contract is based on the consent of the parties thereto. The scope of such consent is not confined to a number of specifically recognized types of transactions. And the contract does not, as a rule, require compliance with any formalities for its validity. These are the three main elements characterizing our general law of contract, and it is obvious that the final and general recognition of the fact that every lawful agreement begets an action (*ex nudo pacto oritur actio*) was of momentous importance for the emergence of the modern concept of contract" (Zimmermann; 1990: 546).

As mentioned by Roskill LJ in *Cehave NV v Bremer Handelgesellschaft MbH,*[1] in English law the general principle is that the law of contract is the same for all contracts:

> "In principle it is not easy to see why the law relating to contracts for the sale of goods should be different from the law relating to the performance of other contractual obligations, whether charter parties or other types of contract. Sale of goods law is but one branch of the general law of contract. It is desirable that the same legal principles should apply to law of contract as a whole and that different legal principles should not apply to different branches of that law."

[1] *Cehave NV v Bremer Handelgesellschaft MbH* 1976 QB 44.

2.1.2.1 Formation of contract

The American Law Institute (1934) provides the following requirements for the formation of an informal contract in the law in the Restatements:

a) A promisor and a promise each of whom has legal capacity to act as such in the proposed contract;
b) A manifestation of assent by the parties who form the contract to the terms thereof, and by every promisor to the consideration of his promise…
c) A sufficient consideration…
d) The transaction… is not void by statute or by special rules of the common law.

That the parties should reach agreement is the first requisite of a contract; "agreement is made when one party accepts an offer made by the other" (Treitel; 1995: 8). In the common law this 'meeting of minds' is known as *consensus ad idem*. To determine the existence of an agreement, offer by one party and acceptance by another must be established, as noted by Lamont J in *Acme Grain Co. v Wenaus:*[2]

> "To constitute a contract there must be an offer by one person to another and acceptance of that offer by the person to whom it is made. A mere statement of a person's intention, or a declaration of willingness to enter into negotiation is not an offer and cannot be accepted so as to form a binding contract."

Furmston (1986) however suggests that few legal systems will treat all agreements as being enforceable contracts. "The elements of simple contract are mutual assent and consideration. If either is lacking, there is no contract, whatever obligation may arise" (Ashley; 1913: 432). As a general rule, a promise is not binding as a contract without being supported by some sort of 'consideration' (that is something valuable in the eyes of the law). Instead a bargain element is deemed as essential for a contract to be enforced by means of the doctrine of consideration in English law.

[2] *Acme Grain Co. v Wenaus* 1917 3 W.W.R. 157.

The American Law Institute (1934) defines Consideration for a promise in the Restatements as:

a) An act other than a promise, or
b) A forbearance, or
c) The creation, modification, or destruction of a legal relation, or
d) A return promise.

Chloros (1968: 139) notes the difference between English law and continental law in that under English law the absence of consideration is fatal to a contract, however in continental law "a mutual exchange of declarations may be binding even though performance may be contemplated by one side to a contract only". Furthermore it is noted by Chloros (1968: 139) that whereas the English law of contract developed through the remedy of *assumpsit* making consideration the test that a bargain was concluded, "continental concepts of contract developed in the middle ages as a result of the influence of rationalism and canon law. The validity of mutual declarations was based upon good faith and the idea that *pacta sunt servanda*".

One of the functions of the doctrine of consideration, as noted by Fridman (1976: 164) is "to provide some test to distinguish between transactions intended by the parties to be legally binding between them and those without such intent or effect, mere moral obligations unenforceable in and by the courts". Consideration has been defined, in *Currie v Misa*,[3] as follows:

> "A valuable consideration in the eye of the law may consist either in some right, interest, profit or benefit accruing to one party or some forebearance, detriment, loss, or responsibility, given, suffered, or undertaken by the other."

In modern common law of contract, each party to the contract must promise or give something in return for another's promise to act; a voluntary or gratuitous act will not suffice. It is obvious that Consideration [is] an element essential to the validity of such contracts [i.e. contracts made

[3] *Currie v Misa* 1875 L.R. 10.

by a doing or giving by one person for the benefit of another in return for a doing or giving by the other], and (as in the case of transactio) the mere promise, made and accepted, to give or to do something, provided that an advantage accrued to the person making the promise, was sufficient to render the contract efficacious (de Villiers; 1924: 121). Furthermore, the contract must show that both parties are bound in some way.

An agreement, though supported by consideration, is not binding as a contract if it was made without any intention of creating legal relations (Treitel; 1995: 150). As stated by Lord Stowell in *Dalrymple v Dalrymple*,[4] contracts:

> "must not be sports of an idle hour, mere matters of pleasantry and badinage, never intended by the parties to have any serious effect whatever."

Moreover the form of a contract is of importance as contracts may be void or unenforceable in modern statute law if they do not adhere to particular requirements.

2.1.2.2 Factors invalidating contract

Since the law requires consent before a contract can come into existence, anything that affects consent between parties, will be relevant in determining whether or not there is a contract (Fridman; 1976). Holmes (1881) notes that the most common grounds for failure of contracts are usually mistake, misrepresentation, or fraud. Factors that invalidate a contract are of relevance to insurance intermediaries as they may be grounds on which to hold the intermediary liable.

An agreement that is vitiated by a mistake which is recognized by common law is not an agreement and consequently will not bind the parties. Furthermore there will be no liability to

[4] *Dalrymple v Dalrymple* 1811 2 Hag Con 54.

perform for either of the parties. Thus mistake, at law, voids a contract. Lord Atkin stated in *Bell v Lever Bros. Ltd,*[5] that:

> "If mistake operates at all, it operates so as to negative or in some cases to nullify consent."

"A representation is a statement of fact made by one party to the contract (the representor) to the other (the representee) which, while not forming a term of contract, is yet one of the reasons that induces the representee to enter into the contract. A misrepresentation is simply a representation that is untrue" (Furmston; 1986: 257). If an agreement has been made on the basis of a misrepresentation, consideration must be given as to whether the misrepresentation was fraudulent or innocent. The agreement remains valid until the person to whom the misrepresentation was made decides to invalidate the contract by treating it as void; if the person voids the contract then their legal rights will depend upon whether there was fraud. If fraud did indeed exist then the remedy will be damages. Should the misrepresentation be innocent however, then the existence of negligence must be established.

In the case of duress (that is where the contract is induced by actual or threatened assault) and undue influence (that is where the consent of the parties is not voluntary but has been unduly influenced by conduct that does not amount to duress) by one party, the contract is voidable at the option of the other party.

Furthermore, as noted by Treitel (1995: 389) the law may refuse to give full effect to a contract on the ground of illegality, *i.e.* because the contract involves the commission of a legal wrong or is in some other way contrary to public policy. The illegality of a contract would thus render that contract null and void. Contracts may be illegal either by statute, common law or contrary to public policy.

[5] *Bell v Lever Bros. Ltd.* 1932 A.C. 161.

2.1.2.3 Parties to the contract and the doctrine of privity of contact

Fridman (1976: 129) notes that as the law stipulates that a contract requires the parties to reach consent on their agreement, only those parties that have the power to consent can be parties to the contract; "this excludes those considered as lacking such power through being under the age of majority or through having a disordered mind". 'Normal' contractual capacity refers to those persons who are mentally competent adult human beings who have full capacity to make contracts. The law does however extend to include artificial persons as amongst those who can attain contractual capacity.

Generally speaking there are two parties to a contract; in the matter under consideration, the insurance intermediary will be one of these parties and the insured or the insurer will be the other. Treitel (1995: 534) notes that the doctrine of privity means that a contract cannot, as a general rule, confer rights or impose obligations arising under it on any person except the parties to it; this leads to the issue of contracts for the benefit of a third party. That only the two parties to the contract have rights and duties in terms of the contract is referred to as the doctrine of privity of contract.

> "An agreement between A and B involves only A and B as parties: there is privity of contract between them. A contract between A and B which requires that A do something for C or that C do something for A creates no privity of contract between A and C or B and C. The contract may mention C and may purport to confer a benefit upon C or impose an obligation upon C, but it cannot result in C's being a party to the contract in the ordinary, usual sense" (Fridman; 1976: 401).

The issue of a contract for the benefit for a third party is a common matter in insurance, for example, A lends his car insured by B to C and B undertakes to indemnify C in the event that C is involved in an accident; A insurers his life with B nominating his wife C as the beneficiary. A dies; what claim does C have against B, and so on. Insurance has more than a passing interest in this matter.

Dowrick (1956) noted that since 1949, in the United Kingdom, in a series of cases in the Court of Appeal, Lord Denning elaborated a doctrine of third party rights arising by way of contract, and in 1954 in a High Court case Mr. Justice Devlin adopted and followed this doctrine.

South African law recognises that third parties may acquire rights from a contract between two other parties in the doctrine of *stipulation alteri*. South African courts follow the view of de Villiers, C.J. in *Tradesman's Benefit Society v du Preez*[6] that:

> "where there is in existence a binding agreement for valuable consideration between the promisor and the promise, there can be no possible injustice in allowing a third person for whose benefit the promise was made and was intended to be made, to recover upon the same."

It should be noted that there is a clear distinction between *stipulatio alteri* and agency; Lee (1953) illustrates this distinction: where A contracts with B with the intention of creating a contractual relationship between B and C, the law of agency will arise (this will be discussed further in Section 2.1.3), however where A and B contract and by so doing confer a benefit on C the *stipulatio alteri* (or the stipulation for the benefit of a third person) will arise. On the question whether a clause in an insurance policy extending the liability of the company to persons other than the insured constitutes a *stipulatio alteri*, Weeramantry (1967: 554) notes that in South Africa such an extension clause is not a *stipulatio alteri* but is 'binding in honour only', as seen in *Old Mutual Fire and General Insurance Co. of Rhodesia (Pvt.) Ltd. v Springer.*[7]

The matter of third party rights within the context of the motor policy has received attention in South Africa.[8] Matters were brought to head in the more recent case of *Unitrans Freight (Pty.) Ltd. v Santam Limited*[9] where the court held that an extension clause of a motor insurance policy obliges the insurer to indemnify authorised users of an insured vehicle, who are not the insured (third parties to the contract) thus constituting an enforceable *stipulatio alteri*. In practice the

[6] *Tradesman's Benefit Society v du Preez* 1887 5 S.C. 269.
[7] *Old Mutual Fire and General Insurance Co. of Rhodesia (Pvt.) Ltd. v Springer* 1963 (2) S.A. 324 (S.R.).
[8] Kahn (1952), Chaskalson (1963) and Reineke (1971)
[9] *Unitrans Freight (Pty.) Ltd. v Santam Limited* (86/03) 2004 ZASCA 20.

stubling block to the smooth practical operation of *stipulatioalteri* is not the doctrine itself but like all contracts requires the other party, in this case the third party, to accept the contractual benefit (*McCullogh v Fernwood Estate Ltd*;[10] *Commissioner for Inland Revenue v Estate Crewe and another)*[11] and in practice this seldom happens. No-one for example when driving a borrowed car first contacts the insurer to notify the insurer that he or she has accepted the extension.

One of the most important exceptions to the doctrine of privity, other than agency, if that of assignment. Assignment is the transfer, to a stranger, *i.e.*, a person who is not a party to the original contract, of contractual rights arising under the contract, so as to permit to assignee to sue the debtor under the original contract in his name, the assignee's own name, with or without the assent of the debtor (Fridman; 1976: 429). It should be noted that assignment, like cession, does not violate the doctrine of privity since a contract is a valuable property right which like all property can be transferred or exchanged.

Adams and Brownsword (1993) note that the courts, notably both in Canada and England, have developed numerous techniques of avoiding privity, as seen in *London Drugs Ltd. v Kuehne and Nagel International Ltd.*[12] where the doctrine of privity of contract was relaxed with La Forest J aptly referring to it as 'that pestilential nuisance'. The strictness of the privity doctrine in English law has not prevented the courts from outflanking it, with both contractual and tortuous devices (Convery; 1999: 771). Beyleveld and Brownsord (1991) further suggest that the doctrine of privity of contract is notorious for its inconvenience.

2.1.2.4 Termination of contract

One of the most obvious situations in which a contract is terminated, resulting in both the parties being discharged from liabilities, is that of performance; where the contract has been performed by both parties. Treitel (1995) notes that it is possible to perform a contract vicariously, this is

[10] *McCullogh v Fernwood Estate Ltd* 1920 AD 204.
[11] *Commissioner for Inland Revenue v Estate Crewe and another* 1943 AD 656.
[12] *London Drugs Ltd v Kuehne and Nagel International Ltd* 1993 1 WWR 1.

done by procuring performance by a third party. Failure or refusal to perform under a contract will result in breach of the contract and will give the other party to the contract the right to claim damages. However non-performance is excusable in certain circumstances. Furmston (1992: 671) notes that non-performance is not the same as breach as it may be excused and that "breach of contract, in the common law sense, is non-excused non-performance".

"*Eodem modo quo oritur, eodem modo dissolvitur*. What has been created by agreement may be extinguished by agreement" (Furmston; 1986: 543). Should the parties to a contract agree to extinguish the existing contract then all rights and obligations under the contract will be terminated. Fridman (1976) notes that a distinction must be made between the different kinds of agreements made by the parties and their resultant effects; one such distinction is that of 'bilateral discharge' (which is available to parties where the contract was wholly or partially executory) and 'unilateral discharge' (where the contract has been performed by one party but not the other).

A contract may be discharged if after its formation events occur that make its performance impossible or illegal; this constitutes the doctrine of frustration. Lando (1992) states that in cases of frustration termination of the contract is automatic; all further liabilities are automatically discharged. Hay (1961: 351) notes that different foreign legal systems generally address the problem of frustration by one of three approaches: "A large group of countries rejects a general doctrine of frustration and affords only limited relief by special legislation in times of crisis. A second group has elaborated doctrines of frustration by judicial construction of code provisions prescribing general standards of conduct, such as good faith. Finally, a third group authorizes, by statute, the judicial adjustment of contracts in accordance with principles of 'equity'".

Furthermore Fridman (1976: 541) notes that in some situations the contract will end "by the virtue of the operation of certain doctrines of law" with or without the desire or intent of either of the parties.

2.1.2.5 Contractual remedies

Where a contract has been breached, the remedy at common law is an action for damages; breach of contract constitutes a civil wrong. Berger (2001) notes that if one party commits a breach of a contractual obligation then not only will remedies be available in the form of damages, but the contract will also be terminated. Johnson (1961: 264) further suggests that the payment of damages for breach of contract does not, on most cases, exempt the party in default from his obligations under the contract. The American Law Institute (1981) states in the Restatements that:

> "Contract liability is strict liability. It is an accepted maxim that pacta sunt servanda, contracts are to be kept. The obligor is therefore liable in damages for breach of contract even if he is without fault and even if circumstances have made the contract more burdensome or less desirable than he had anticipated."

Furmston (1986) notes that a claim for damages raises two important questions: what kind of damage is the plaintiff entitled to recover as compensation, and by what principles must the damages be evaluated and quantified in terms of money? To the first question, the decision in *Hadley v Baxendale*[13] defined the kind of damage that is the appropriate compensation; the decision was concerned with the 'remoteness of damage'. The second question is often referred to as the 'measure of damages' and the principle adopted by the courts is that of *restitutio in integrum*; the plaintiff should be restored to the position he occupied had the damage not occurred. David (1935: 64) notes that the damage caused by the breach, according to the *doctrine*, must be estimated as at the time when the breach occurs.

At common law the only remedy available for the breach of contract was damages, however equitable remedies do also exist. Fridman (1976: 593) notes that equitable remedies are:

> "discretionary and they depend for their availability upon (a) the conduct of the plaintiff, i.e., his own performance of, or willingness to perform, his contractual obligations (b) the

[13] *Hadley v Baxendale* 1854 9 Exch 341.

> merits of the plaintiff's case, i.e., the justice and wisdom of granting the desired enforcement of the contract (c) the suitability of the remedy (d) whether damages would be an adequate way of dealing with the situation".

Equitable remedies include, amongst others, specific performance and injunction.

Furthermore Treitel (1995: 944) notes that a party who has wholly or in part performed his side of the contract and has not received the agreed counter-performance in full may sometimes be entitled to restitution in respect of his own performance. Posner (2008) suggests that courts will sometimes award restitution damages when breach of contract is wilful.

A party to a contract may also attain relief from that contract through rescission; that is "declare that the contract is a nullity and not binding upon the parties, in certain circumstances, when it would be inequitable for the other party to hold the one claiming rescission to the original bargain" (Furmston; 1986: 606). Another remedy in equity is that of rectification, where the courts can vary the terms of a written document.

Fridman (1986: 633) further notes that in modern times "legislatures have been compelled to intervene and create remedies (and sometimes rules of law) which enable courts to ameliorate the situation of parties who have contracted unwisely, though not in any way that would invite the application of common law or equitable principles of relief".

The Columbia Law Review Association (1957: 704, 708) also suggests that "whether the contract has been breached – a question also governed by the *lex loci solutionis* [which has generally been used to determine whether certain acts will be deemed impossible so as to constitute sufficient excuse for non-performance, whether termination of a contract constitutes breach, and whether the illegality of the performance will serve as a successful defense] according to the Restatement [American Law Institute (1934)] – may often depend on an interpretation of terms, a matter traditionally controlled by the law governing validity"

2.1.3 Law of agency

It stands to reason that, after the law of contract, the law of agency is of central importance to the insurance intermediary. Müller-Freienfels (1964) notes that the first rules of agency appeared no earlier than from the twelfth and thirteenth centuries onwards and that Roman law never developed a complete theory of agency; "the Romans never acknowledged a general rule in their private law which declared that a person, acting as an intermediary, should be capable of creating a valid contractual or commercial relations between the principal and a third party" Müller-Freienfels (1964: 193-194). Zimmermann (1990) further notes that although certain situations in which a person could act through a middleman were recognized, no comprehensive legal institution of agency ever developed.

Fridman (1971: 8) describes the agency relationship as follows: Agency is the relationship that exists between two persons when one, called the agent, is considered in law to represent the other, called the principal, in such a way as to be able to affect the principal's legal position in respect of strangers to the relationship by the making of contracts or the disposition of property.

As noted by Steffen (1977: 26) the essentials of agency are as follows: "First, the relation is a *consensual* one; an agent *agrees*, or at least *consents* to act under the *direction* or *control* of the principal. Second, the relation is a *fiduciary* one; an agent agrees to act *for* and *on behalf* of the principal. He is in no sense a proprietor entitled to *gains* of enterprise nor is he expected to carry the *risks*".

Rasmusen (1996: 2) notes that when the American Law Institute began to compile the influential summaries of the common law known as the 'restatements', the Restatement of Agency was important enough to be second in the series (after contracts). According to the American Law Institute (1958: §1.1) agency is: the fiduciary relationship which results from the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control, and consent by the other so to act.

There are four ways by which the principal-agent relationship is established: by an agreement between two parties, by ratification, by estoppel, and by operation of law. In most instances relating to insurance intermediaries, the consequences attributed by the law to the relationship between the principal and the agent, stem from a contract. "The rules which determine whether or not the company is bound by such contracts… are those of the law of agency" (Barak, 1969: 847).

Duska (2005: 25) suggests that legally, any insurance agent who signs a contract with a company acts as an agent for that company, and agency law requires the agent to act on behalf of the principal, which in this case is the [insurance] company. This view is however suspect since it assumes an agent of the whole and not an agent of a transaction. However this may not always be the case as it is possible to be bound, not as a whole but merely by specific transactions; for example, the insurance intermediary who is mandated to procure insurance on the behalf of an insured can be the agent of the insured. Thus the insurance intermediary may be the agent of both the insured and the insurer but for different transactions. It is difficult to accept anyone can be the agent of both parties for the same transaction, yet this problem has arisen with respect to Lloyd's agents.

When considering how the general principles of the law of agency are applied to insurance business, and more specifically to the insurance intermediary, three relationships must be considered: the relationship between the principal and the agent, the relationship between the principal and third parties, and the relationship between the agent and third parties.

2.1.3.1 The relationship between the principal and the agent

Not only does an agent have certain rights against his principal, but he also has certain duties that must be performed. The agents' failure to fulfill his duties (mandate) will result in a breach of duties (mandate) and certain consequences may ensue.

An agent has the right to be remunerated by the principal. The agent also has the right to indemnity whereby he can be reimbursed for any sums expected on the principal's behalf.

Furthermore the agent has the right to claim a lien; "the agent of the insured, who, on payment of the premiums receives the policy from the insurers, may retain it and refuse to hand it over to the assured until the amount of the premium has been paid to him by the assured" (Ivamy, 1975: 487).

Moreover, the agent has certain duties that must be performed; the main duties that the agent owes the principal are discussed below.

The agent has a duty to perform whatever he has undertaken to perform in terms of the contract. This amounts to a duty to carry out the transaction which was made with the principal, as seen in *Turpin v. Bilton:*[14]

> "The agent was appointed under a contract to insure the principal's ship. He failed to do so, the ship was lost, and the principal was therefore uninsured at the time. It was held that the agent had been guilty of a breach of contract, for which he is liable."

The agent does not however have to perform the transaction if it is illegal or null and void by common law or statute.

The American Law Institute (1958: §33) notes in the Restatements that there is a 'general principle of interpretation' which states that:

> "An agent is authorized to do, and to do only, what is reasonable for him to infer that the principal desires him to do in the light of the principal's manifestations and the facts as he knows or should know them at the time he acts."

There is a duty upon the agent to carry out his instructions, or manadte and "the agent, in the performance of the undertaking, must act in accordance with the authority which has been given [to] him. He must obey instructions contained in his express authority (as long as they are lawful); or he must act in accordance with the general nature of his business, that is to say within

[14] *Turpin v Bilton* 1843 5 Man & G. 455.

his implied authority; or he must act in accordance with trade, or other customs and usages, where they can apply in the performance of the undertaking, that is to say when he can act within his usual or customary authority" (Fridman, 1971: 122).

The agent has a duty to perform the undertaking with reasonable and proper care, skill, and diligence. Where the agent is a professional, for example a broker, the standard of care is measured by persons of experience in his profession, as noted by Tindal C.J. in *Chapman v Walton:*[15]

> "The action is brought for the want of reasonable and proper care, skill and judgment shown by the defendant under the certain circumstances in the exercise of his employment as a policy-broker. The point, therefore, to be determined, is not whether the defendant arrived at a correct conclusion upon reading the letter, but whether, upon the occasion in question, he did or did not exercise a reasonable and proper care, skill and judgment. This is a question of fact, the decision of which appears to us to rest upon this further enquiry, *viz*. whether other persons exercising the same profession or calling, and being men of experience and skill therein, would or would not have come to the same conclusion as the defendant."

Furthermore, the agent has a duty to account to the principal for money that is received on behalf of the principal. It is the duty of the agent, when employed to receive payment on his principal's behalf, to act with due diligence in collecting the amounts payable to his principal and to pay over to the principal such sums as he may have received in the course of his employment (Ivamy, 1975: 493). Macey and O'Hara (1997) note that the common law of agency states that where an agent makes a profit in connection with any transactions conducted on behalf of the principal, the agent has a duty to give such profits to the principal. This is also mentioned in Section 388 of the Second Restatement of Agency by the American Law Institute (1958).

If an agent breaches any of his duties to his principal all his rights against his principal are forfeited. The agent will also be liable for all losses sustained by the principal that resulted from the breach of duty. Moreover the agent can be dismissed immediately.

[15] *Chapman v Walton* 1833 10 Bing. 57.

Fridman (1971: 133) notes that in addition to those duties which are implied by the law into the agreement creating the agency relationship, there are others which stem from the fact that the agency relationship is one of trust, even though not strictly a relationship of trustee and beneficiary. These duties are known as fiduciary duties. The American Law Institute (1958: §387-§396) however refers to these duties as "duties of loyalty" in the Restatements. These duties suggest that the agent must not let his own personal interests' conflict with those duties he owes his principal. Reynolds (1985) however notes that there still exists controversy as to how these duties should be formulated, their extent in particular situations, as well as the remedies by which they may be enforced.

2.1.3.2 Relationship between the principal and third parties

Generally the principal is liable to the third party for any act performed by the agent *within* the agent's authority. Since the agent acts on behalf of the principal, dealings with an agent acting within the scope of his delegated authority are treated as dealings directly with the principal (Fairfield, 2001: 228).

The principal will not be affected by any acts performed by the agent in excess of his authority unless the principal wishes to adopt what the agent has done by means of the doctrine of ratification. Ratification is defined by the American Law Institute (1958: §82) in the Restatements as: the affirmance by a person of a prior act which did not bind him but which was done or professedly done on his account whereby the act, as to some or all persons, is given affect as if originally authorised by him.

Thus the actual authority of the agent is, as noted by Reynolds (1985: 92), "the authority which the principal has given the agent wholly or in part by means of words or writing… or is regarded by the law as having given him because of the interpretation put by the law on the relationship and dealings of the two parties" or by virtue of the doctrine of ratification. Diplock L.J. in *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd.*[16] stated that:

[16] *Freeman and Lockyer v Buckhurst Park Properties (Mangal) Ltd.* 1964 1 All E.R. 630.

> "An 'actual' authority is a legal relationship between principal and agent created by a consensual agreement to which they alone are parties. Its scope is to be ascertained by applying ordinary principles of construction of contracts, including any proper implications from the express words used, the usages of the trade, or the course of business between the parties."

When dealing with the issue of the principal's liability to third parties, the nature and extent of the agent's authority must be considered. Liability will arise only if the agent acts within his express, implied, usual, or apparent authority.

An agent's authority is express when it is limited to the terms of the agreement or contract. Therefore if an agent is contracted to effect insurance on behalf of a proposed assured then the principal is bound by any policy which is in accordance with the agent's instructions. Lord Denning M.R. in the case of *Hely-Hutchinson v Brayhead Ltd*.[17] stated that:

> "Actual authority, express and implied, is binding as between the company and the agent, and also as between the company and others, whether they are within the company or outside it."

Fridman (1971: 90) notes that "in the *Freeman* case [as above], Willmer L.J. differentiated express authority from implied authority, an instance of the latter occurring if the agent in question had been appointed by the company of which he had been a director to some office which carried with it authority to make such a contract of the kind involved on behalf of the company… This is a valid use of the term 'implied authority', for it shows that the contract of agency is to be interpreted in the light of what is necessary to imply into it in order to make it effective".

Furthermore Rasmusen (1996:3) suggests that implied authority is where the principal has entered into an explicit agreement to employ the agent, and although he has not specifically

[17] *Hely-Hutchinson v Brayhead Ltd*. 1967 3 All E.R.

authorized the particular action at issue, the agent can reasonably infer that authority for that action has been delegated to him. An important feature of implied authority is that the consent of the principal is required. Brown (1992) further suggests that the agent's implied authority will extend to all acts that are incidental to and necessary for the execution of express authority, which consequently expands such express authority.

Usual authority is the authority which an agent in a particular profession which that specific agent is employed should possess. Thus, in the case of insurers, an agent may be employed to negotiate the terms of a proposal and to induce the proposed assured to make a proposal which the insurers are willing to accept (Ivamy, 1975: 499).

Fridman (1971: 92) notes that apparent authority "is an authority which an agent has not been given by the principal, but which the law regards the agent as possessing notwithstanding the principal's lack of consent to his exercising such authority. The reason for this is that the principal, by his conduct, has allowed the agent to appear to have authority, or to have a greater authority than was in fact given him by the principal". Apparent authority is further explained by Diplock L.J. in the *Freeman* case (as above):

> "… a legal relationship between the principal and the contractor [i.e. a third party] created by a representation, made by the principal to the contractor, intended to be and in fact acted on by the contractor, that the agent has authority to enter on behalf of the principal into a contract of a kind within the scope of the 'apparent' authority, so as to render the principal liable to perform any obligations imposed on him by such contract."

The concept of 'inherent agency power' was formally introduced by the American Law Institute in the Second Restatement. Rasmusen (1996: 4) notes that it is a term intended to cover the liability that arises where the agency relationship may give an agent the power to harm a third party even if there is no manifestation by the principal that the agent is acting on his behalf. The American Law Institute (1958: §8A) states that:

> "Inherent agency power is a term used in the restatement of this subject to indicate the power of an agent which is derived not from authority, apparent authority or estoppels, but solely from the agency relation and exists for the protection of persons harmed or dealing with a servant or other agent."

Acts that fall outside the scope of the agent's authority (whether the agent has no authority or his express, implied, usual, or apparent authority are not so far extended) do not bind the principal.

It is possible that the principal may be deemed to have received certain information which has in fact only been received by the agent. Scordato (2004: 131) notes that the 'imputed knowledge rule' legally charges the principal with information obtained by the agent within the scope of the agent's service for the principal; thus the principal is seen as having received all information even if it is clear that the agent did not provide the principal with such information.

2.1.3.3 The relationship between the agent and third parties

An agent will have certain rights and liabilities under the contract made with the principal. An agent cannot, as a general rule, enforce a contract which he has effected on behalf of a named principal or of a principal whose existence he has disclosed to the third party but whose name he has not given (Ivamy, 1975: 526).

Reynolds (1985: 424) notes that in the absence of other indications, when an agent makes a contract, purporting to act solely on behalf of a disclosed principal, whether named or unnamed, he is not liable to the third party on it. As stated by Wright J in *Montgomerie v U.K. Mutual S.S. Assn. Ltd.*:[18]

> "There is no doubt whatsoever as to the general rule as regards an agent, that where a person contracts as agent for as principal, the contract is the contract of the principal and not that of the agent; and, prima facie, at common law the only person who may sue is the principal and the only person who can be sued is the principal."

[18] *Montgomerie v U.K. Mutual S.S. Assn. Ltd.* 1891 1 Q.B. 370.

> "In this regard, it should be remembered that the doctrine of the *undisclosed principal* pursuant to which, whenever the agent acts in his own name without disclosing to the third party that he is acting as an agent, he is liable to the third contracting party and, the later disclosure of the existence and identity of the principal does not exclude the liability of the agent. However, the third party may act by either choosing to take action against the 'disclosed' principal or against the agent (*election*), from which it can be inferred that the doctrine recognizes the legal effects of agency in the case of an agent who acts in the interests of a principal although his existence has not been disclosed in any way" (De Miglio, Onida, Romano, Santoro, 2002: 24-25).

Müller-Freienfels (1957: 178) further notes that it is a fundamental principle of the Anglo-American law of agency that an undisclosed principal may sue and be sued on a contract made by an agent with a third party, provided that the agent has authority to make the contract.

The agent can also be sued by a third party for breach of warranty of authority if he had no authority when entering the contract and the principal either refuses or fails to ratify the contract.

Furthermore it is possible for the agent to be liable in tort to third parties. Hodgin (1987: 18) notes that apart from the principal's legal liability for his agent it is possible to hold the agent personally liable.

2.2 Law of delict

Most liability risks that concern insurers are founded in the law of delict. In theory however the liability of the intermediary is usually in contract. It is the role of delict to indicate which interests are recognized by the law, the circumstances under which there exists protection against infringement, and how these disturbances may be restored.

The fundamental premise in law is that harm lies where it falls; each person bears the damage he suffers (*res perit domino*). However circumstances exist where the burden of damage shifts from one individual to another resulting in the latter having to bear the losses of the former's damage

or provide compensation for it. Thus the law of delict determines when a person is obliged to bear the damage he has caused another or when he may incur a civil liability for such damage.

Neethling, Potgieter and Visser (2006: 3) define delict as an "act of a person that in a wrongful and culpable way causes harm to another". For liability to attach in delict, five elements must be present: conduct, wrongfulness, fault, causation, and damage. Should any of these elements be missing, delict is not established and consequently there will be no liability. However, Valsamakis, Vivian and du Toit (1992: 207) note that, in practice, it seldom occurs that all five elements are investigated in the same case.

It follows that delictual liability is governed by a generalizing approach whereby generalizing principles regulate delictual liability; these rules apply irrespective of which individual interest, for example the human body, a trademark, or privacy, is impaired. This approach of South African law is apparent in the controversial *dictum* of *Perlman v Zoutendyk:*[19]

> "Roman-Dutch law approaches a new problem in the continental rather than the English way, because in general all damage caused unjustifiably (*injuria*) is actionable, whether caused intentionally (*dolo*) or by negligence (*culpa*)".

The English and Roman laws of delict however rely on a casuistic approach where the law of torts consists of a group of separate delicts, that is torts or *delicta*, each of which have their own set of rules.

Zimmermann (1990: 907) provides the following distinction between the terms 'delict' and 'tort': "'Delict'… is the civilian term generally used to designate a civil (as opposed to criminal) wrong. Its common-law counterpart is 'tort'… Delict and tort are functional equivalents, since both of them refer to certain wrongful acts which the law is prepared to redress… The continental law of delict presents the picture of a coherent body of rules based on general principles and abstract concepts… 'Tort' does not constitute a coherent body of law… but is no more than a sum total of a variety of individual torts… Each of these specific torts is still

[19] *Perlman v Zoutendyk* 1934 CPD 151 155.

regarded as an independent cause of liability, each has its own constituent elements, and each protects a special interest from being inferred with."

In South African law the generalizing approach is subject to a qualification; there is a distinction made between delicts that cause patrimonial damage (*damnum injuria datum*) and those that cause injury to personality (*injuria*). These form two actions which are the basis of the law of delict. Firstly the *actio legis Aquiliae*, or the Aquilian action, is where the damages for the wrongful and culpable causing of patrimonial loss can be claimed, for example the loss of income, and secondly the *actio injuriarum* relates to the satisfaction for the wrongful and intentional injury to personality, for example defamation. As stated by Thirion J in *Edouard v Administrator Natal:*[20]

> "In present day Roman-Dutch law the *actio injuriarum* and the *actio legis Aquiliae*, in its extended form, cover almost the whole field of delictual liability."

Another important action is the *action for pain and suffering* where it is possible to claim compensation as a result of the wrongful and negligent impairment of bodily or physical-mental integrity which is of German, not Roman origin, and was introduced at a later stage of the development of the law.

2.2.1 Historical development of delictual liability

Zimmermann (1990: 2) notes that the early roots of liability in private law lie in what we today call delict. There was however no general definition of what a delict is in ancient law. South African law of delict is based on three pillars: the *actiolegisAquiliae*, the *acti injuriarum*, and the later German addition, that of the *action for pain and suffering*. Due to the changes in the law of delict over the last few decades it is necessary to consider the historical development of the law of delict to ascertain the implications of these actions.

[20] *Edouard v Administrator Natal* 1989 2 SA 368 (D) 389.

2.2.1.1 *ActiolegisAquiliae*

The liability for patrimonial damages, *damnuminiuria datum*, is one of the most significant sections of Roman law that still exists in South African law today. It was based on a Lex derived from a (*plebiscitum*) from 287 BC known as the *LexAquilia*. The *Lex* constituted three chapters, of which only two are still relevant today. From these two chapters the *Lex* was only applicable to certain forms of damage to corporeal things. Furthermore the *Lex* was only available to the owner where there had been physical damage caused by the direct application of force.

In time the Aquilian action was so considerably extended that Aquilian liability could arise due to any physical infringement of a thing. Furthermore, the wrongdoer had to compensate for the damage that had been caused to the thing itself as well as patrimonial damages that resulted from the wrongful act.

Though the basis of liability seemed to expand, it still remained limited in that it had to relate at least to fault and physical damage with a connection between the two. This paved the way for the Aquilian action to be a general remedy for all patrimonial losses wrongfully caused.

The Aquilian action underwent further extensions within Roman-Dutch law; however the developments did not indicate that the Aquilian action in Roman-Dutch law had developed into a general remedy for the culpable and wrongful causing of patrimonial damage.

A description of the extension of the Lex Aquilia in Roman-Dutch law is provided by De Villiers CJ in *Cape of Good Hope Bank v Fischer*:[21]

> "It appears from both these authors [Voet and Matthaeus] that in their time the Aquilian law had received an extension by analogy to a degree never permitted under Roman law. The action in factum was no longer confined to cases of damage done by a person in consequence of the wrongful acts of another."

[21] *Cape of Good Hope Bank v Fishcer* 1886 4 SC 368 on 376.

In modern South African law Aquilian liability arises from every culpable and wrongful act that causes patrimonial damage. Despite earlier cases, which recognised only physical injury to found Aquilian liability, it has been established in modern law that compensation for 'pure' economic loss may in principle be claimed *ex legeAquilia* but the basis on which the claim rests is still problematic. Booysen J stated in *Coronation Brick (Pty) Ltd v Strachan Construction Co (Pty) Ltd.*[22] that:

> "The legal basis of the plaintiff's claim is the *lexAquilia*. In essence the Aquilian action lies for patrimonial loss caused wrongfully (or unlawfully) and culpably. Although the contrary view had long been held by many authorities, it seems clear that the fact that the patrimonial loss suffered did not result from physical injury to the corporeal property or person of the plaintiff, but was purely economic, is not a bar to the Aquilian action."

This matter is discussed in greater detail below.

Generally there is a strong tendency in South African case law to recognize Aquilian liability for all patrimonial loss caused wrongfully and culpably. As held by Innes JA in *Union Government (Minister of Railways and Harbours) v Warneke,*[23] the extent of liability has expanded considerably in modern law:

> "The position of our law with regard to negligence to-day is the result of the growth and the regulated expansion of the original provisions of the *LexAquilia*. Crude and archaic in some respects, their operation was gradually widened by the application of the *utilisactio*, and by the interpretation of the Roman jurists. The broadening process was continued by Dutch lawyers on the same lines; and there is no reason why our Courts should not similarly adapt the doctrine and reasoning of the law to the conditions of modern life, so far as that can be done without doing violence to its principles."

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[22] *Coronation Brick (Pty) Ltd v Strachan Construction Co (Pty) Ltd* 1982 4 SA 371 (D) 377.
[23] *Union Government (Minister of Railways and Harbours) v Warneke* 1911 AD 657 664-665.

South African courts however adopted a conservative approach to expanding the Aquilian action and, according to *Lillicrap, Wassenaar and Partners v Pilkington Brothers (SA) (Pty) Ltd*.,[24] an extension will only be permitted if it is justified by policy considerations:

> "South African law approaches the matter in a more cautious way… and does not extend the scope of the Aquilian action to new situations unless there are positive policy considerations which favour such an extension."

2.2.1.2 *Actioinjuriarum*

The violation of the rights of people to their person (such as assault, imprisonment, insult or defamation, corpus et dignitas) in such a way that they give rise to damages is referred to as the violation of personality rights; the delictual action is that of *injuria*.

The *actioinjuriarum* was based on the Twelve Tables in about 450 BC. In Roman law each wrong against a person was treated as an *injuria* and a fixed monetary penalty was imposed whereby the victim could recover from the wrongdoer. By the second century BC, this system was replaced by a series of praetorian edicts.

Roman law concerning the liability to personality was adopted almost without change in South Africa and thus is of significant relevance to the law. In Roman law the *injuria* concept was developed into a general delict which intended to protect personality interests. However the *actioinjuriarum* did not protect the personality in its entirety but protected against the intentional infringement of a person's *corpus* (person), *fama* (reputation) or *dignitas* (dignatas).

Roman-Dutch law of delict followed that of the Roman law, remaining almost unaltered. There was however development in the protection of personality whereby the *actio injuriarum* was replaced with two actions: *amende profitable* and *amende honorable*. The former action dealt

[24] *Lillicrap, Wassenaar and Partners v Pilkington Brothers (SA) (Pty) Ltd* 1985 1 SA 475 (A) 500 503-504.

with the recovery of satisfaction and the latter gave the injured person the right to demand that the wrongdoer withdraw his words and admit guilt.

A distinction can be made between the *actioinjuriarum* and the *actiolegisAquiliae* in that the *actioinjuriarum* requires fault or intent (*animus injuriandi*). The courts have judged a man's intentions by his actions as noted by Solomon J in *Whittaker v Roos*:[25]

> "It is not necessary in order to find that there was *animus injuriandi* to prove any ill-will or spite on the part of the defendants toward the plaintiff; and it is quite immaterial what the motive was or that the object which the defendants had in view was a laudable one. It is sufficient that the injuries suffered by the plaintiffs were inflicted by the defendants, not accidentally or negligently, but with deliberate intention."

In South African law the delict, Innes J in *R v Umfaan*[26] states that an *injuria*:

> "is a wrongful act designedly done in contempt of another, which infringes his dignity, his person and his reputation. If we look at the essentials of *injuria* we find… that they are three. The act complained of must be wrongful; it must be intentional; and it must violate one or other of those real rights, those rights in *rem*, related to personality, which every free man is entitled to enjoy."

2.2.1.3 Action for pain and suffering

Under Roman law, no compensation could be claimed for the negligent causing of bodily injuries. Claims for pain and suffering emerged in Germanic law. Roman-Dutch law, pain, suffering, and bodily disfigurement that resulted from physical injuries followed the Germanic precedent and began to allow an action for pain and suffering.

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[25] *Whittaker v Roos* 1912 AD 92.

[26] *R v Umfaan* 1908 TS 62 66.

The evolution of the action for pain and suffering from its rudimentary beginnings as a means of compensating a person for pain, suffering and disfigurement, to the developed action which now includes damages for loss of amenities of life and loss of expectation of life, was to some extent influenced by the English law (Burchell, 1993, 12-13). South African courts developed this action, in light of English law, to the extent of the protection of physical integrity of a person in its entirety.

2.2.2 General principles

Five elements must be present for liability to attach in delict, failing this delict is not established and consequently there will be no liability. Furthermore common law doctrines of the law of delict have changed considerably over the past few decades and thus it becomes pertinent to explore the implications of these.

2.2.2.1 Conduct

One of the prerequisites of delictual liability is that of conduct; a person must cause harm or damage to another by means of an act or conduct. Neethling et al (2006:23) define conduct as a voluntary human act or omission.

In Roman law only a positive act was actionable provided that it set in motion a sequence of events which resulted in harm suffered by the plaintiff; without this positive there was no liability. Over a period of considerable time, this changed to include omissions as part of the notion of conduct. The case of *Halliwell v Johannesburg City Council*[27] changed the law considerably by changing the nature of the act. Prior to this case the act had to be the proximate cause of harm, that is it had to set in motion the sequence of events that would cause harm. The act and harm were contemporaneous. This however changed in the case of *Cape Town Municipality v Paine*[28] which established that prior positive act, no longer contemporaneous with

[27] *Halliwell v Johannesburg City Council* 1912 AD 659.
[28] *Cape Town Municipality v Paine* 1923 AD 207.

the harm, was sufficient for liability to exist. It was thereafter accepted that prior positive conduct was sufficient to establish liability and the nature of this prior conduct was not such that it itself could cause harm.

In *Blore v Standard General Insurance Co Ltd en 'n ander*,[29] the issue of whether liability could arise from a mere omission, that is, in the absence of prior conduct, was addressed. Here the court found that there was a duty on the defendant to act based on their prior conduct. The only category of liability for omissions for which there is clear authority is 'prior conduct'; much of this authority goes so far as to imply that it is indeed the only category of liability for omissions at all (Boberg, 1972: 212).

In 1975 the case of *Minister of Police v Ewels*[30] found the court abandoning the narrow concept of prior conduct and introducing a broader concept, that of wrongfulness whereby courts had a much wider discretion. The court ruled that:

> "Our law has developed to the stage where an omission can be regarded as wrongful also where the circumstances of the case are such that the omission not only evokes moral indignation, but also the legal convictions of the community require the omission be regarded as wrongful and that the loss suffered be compensated by the person who failed to act positively."
>
> (translation from Afrikaans)

Furthermore the court decided that a person could be liable in accordance with the legal convictions of society but failed to lay down an objective test to establish how these convictions are to be determined.

[29] *Blore v Standard General Insurance Co Ltd en 'n ander* 1972 2 SA 89 O.
[30] *Minister of Police v Ewels* 1975 3 SA 590 A.

In modern case law it is evident that the act as known in Roman and Roman-Dutch law has all but disappeared. It now seems to be at the discretion of a judge to determine what constitutes an act.

2.2.2.1.1 Omissions

As a general rule the law of negligence did not and does not impose a duty of care in respect of failure to act. If such liability is to exist, it would be a new form of liability and have to be introduced. Even though Lord Atkin makes mention of "acts and omissions" in the *Donoghue* case, as above, English law has been reluctant to deviate from the historical position and impose liability for omissions. In English law historically there is no general duty to prevent an injury. For example, there is no duty upon a person who sees another drowning to save the other; here the law would impose no liability on that person who chose not to save the other.

Lord Hoffmann highlights why duty of care should be restricted in cases of omissions in *Stovin v Wise*[31]:

> "There are sound reasons why omissions require different treatment from positive conduct. It is one thing for the law to say that a person who undertakes some activity shall take reasonable care not to cause damage to others. It is another thing for the law to require that a person who is doing nothing in particular shall take steps to prevent another from suffering harm from the acts of third parties or natural causes. One can put the matter in political, moral or economic terms. In political terms it is less an invasion of an individual's freedom for the law to require him to consider the safety of others in his actions than to impose upon him a duty to rescue or protect. A moral version of this… Why should one be liable rather than another? In economic terms, the efficient allocation of resources usually requires an activity should bear its own costs… Except in special cases English law does not reward someone who voluntarily confers a benefit on another. So there must be some special reason why he should have to put his hand in his pocket."

[31] *Stovin v Wise* 1996 AC 923.

However it becomes important to clarify what is meant by an omission. Negligence generally implies not having done something; negligent conduct consists in acts or omissions. "It has been said that negligence always consists in omission. This arises from confusion between negligence and carelessness. Carelessness does consist in an omission to take thought about the consequence of one's conduct; and it is that omission which has been mistaken for negligence in the legal sense" (Terry; 1915: 41-42).

Lord Goff mentions the exceptions to no liability for omissions in his dictum in *Smith v Littlewoods Organisation Ltd.*[32]:

1) Where there is a relationship creating an assumption of responsibility.
2) Where there is an existing relationship with the wrongdoer involving control.
3) Where there is a creation of or failure to remove a danger which is then used by the third party.

As noted by Lord Keith in *Yuen Kun Yeu v Attorney General of Hong Kong*[33], for liability to be imposed for negligent omissions there must be circumstances which:

> "Have the effect of bringing into being a relationship apt to give rise to a duty of care. Foreseeability of harm is a necessary ingredient of such a relationship, but it is not the only one. Otherwise there would be liability in negligence on the part of one who sees another about to walk over a cliff with his head in the air, and forbears to shout a warning."

2.2.2.2 Wrongfulness

An act itself, as previously discussed, is insufficient to give rise to delictual liability. A loss must be caused in a wrongful manner for liability to attach. 'Wrongful' may be expressed as unreasonable or legally reprehensible (Neethling *et al*; 2006).

[32] *Smith v Littlewoods Organisation Ltd*. 1987 2 WLR 480.
[33] *Yuen Kun Yeu v Attorney General of Hong Kong* 1988 AC 175.

An act is only delictually wrongful when harmful consequences ensue. This is seen in the judgment of Van Reenen J in *Thomas v BMW South Africa (Pty) Ltd:*[34]

> "There can be no delict in the absence of a wrongful act or omission on the part of a wrongdoer. An act or omission can be characterized as wrongful only if it results in *damnum*. Until that happens an act or omission constitutes no more than 'negligence in the air'. Wrongfulness is not simply an attribute of a wrongdoer's conduct but a function of that conduct together with its consequences in relation to a particular person".

In Roman-Dutch law acting wrongfully meant acting contrary to the law which prohibited damage to property. In modern law, to establish wrongfulness two issues must be considered: if a legally recognizable interest has been infringed and if that interest was prejudiced then legal norms must be used to determine whether the infringement was caused in a legally reprehensible manner.

The test for wrongfulness is set out by *the legal convictions of the community* or the *boni mores* criterion. This is an objective test based on reasonableness as expressed by the court in *Coronation Brick (Pty) Ltd v Strachan Construction Co (Pty) Ltd:*[35]

> "[I]n any given situation the question is asked whether the defendant's conduct was reasonable according to the legal convictions of the community".

Neethling *et al* (2006) note that the test asks the following question: according to the legal convictions of the community and in light of all the circumstances of the case, has the defendant infringed the interests of the plaintiff in a reasonable or an unreasonable manner?

When applying the *boni mores* criterion to the law of delict the court in *Van Eeden v Minister of Safety and Security (Women's Legal Centre Trust, as amicus curiae)*[36] found that:

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[34] *Thomas v BMW South Africa (Pty) Ltd* 1996 2 SA 106 (C) 120.
[35] *Coronation Brick (Pty) Ltd v Strachan Construction Co (Pty) Ltd* 1982 4 SA 371 (D) 377.

> "In applying the concept of the legal convictions of the community the Court is not concerned with what the community regards as socially, morally, ethically, or religiously right or wrong, but whether or not the community regards a particular act or form of conduct as delictually wrong."

2.2.2.3 Fault

In Roman-Dutch law a person was at fault if, when he committed an act he either knew (dolus) that the consequences of his actions were unlawful or a reasonable man in his position could foresee (culpa) that the consequences would be unlawful. Thus if a person by his positive conduct caused injury to someone he could still avoid liability if a reasonable man in his position would not have foreseen the harm his act would bring about and if he did he would not have taken steps to prevent the harm.

In law two forms of fault are recognized: intention (*dolus*) and negligence (*culpa*).

Grosskopf JA stated in *Dantex Investment Holdings (Pty) Ltd v Brenner*[37] that:

> "[I]t is now accepted that *dolus* encompasses not only the intention to achieve a particular result, but also the consciousness that such a result would be wrongful or unlawful."

Intention thus has two elements: direction of the will and consciousness of wrongfulness. Furthermore there are three forms of intent (dolus):

- Direct intent (*dolus directus*) – the wrongdoer knows that what he is doing is wrong but does it nonetheless; he desires a particular consequence of his conduct.

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[36] *Van Eeden v Minister of Safety and Security (Women's Legal Centre Trust, as amicus curiae)* 2003 1 SA 389 (SCA) 395-396.
[37] *Dantex Investment Holdings (Pty.) Ltd. v Brenner* 1989 1 SA 390 (A).

- Indirect intent (*dolus indirectus*) – the wrongdoer directly intends an outcome from his conduct but is aware that other wrongful consequences will inevitably occur.
- *Dolus eventualis* – the wrongdoer foresees the real possibility of harm but nevertheless performs the act which results in the consequence in question.

Negligence refers to situations where an individual fails to adhere to the standard of care legally required of him. As seen in the well-known *dictum* of Holmes JA in *Kruger v Coetzee,*[38] which set out the general test for negligence which arises if:

> (a) a *diligens paterfamilias* in the position of the defendant –
>
> (i) would foresee the reasonable possibility of his conduct injuring another in his person or property and causing him patrimonial loss; and
>
> (ii) would take reasonable steps to guard against such occurrence; and
>
> (b) the defendant failed to take such steps.

Neethling *et al* (2006) note that this general test of negligence, namely that of a reasonable person in the position of the wrongdoer, cannot be applied when the conduct of the defendant involves the application of professional expertise. Instead, the test of negligence has to be refined to that of a reasonable expert and not the universal reasonable person. In this instance, the case of *Van Wyk v. Lewis*[39] which involved a professional liability case against a doctor, states:

> "And in deciding what is reasonable the court will have regard to the general level of skill and diligence possessed and exercised by the members of the branch of the profession to whom the practitioner belongs. The evidence of (other) practitioners is of the greatest assistance in estimating the general level".

Modern law has evolved in such a way that the nature of fault has been changed from merely an element of defence to a cause of action, as in the case of the tort of negligence; liability may arise

[38] *Kruger v. Coetzee* 1966 2 SA 428 (A) 430.
[39] *Van Wyk v Lewis* 1924 AD 438.

if a person does not take the steps to prevent injury even if that person did not in any way cause the injury, as seen in *Langley Fox Building Partnership (Pty) Ltd v De Valence*[40] and *Butters v Cape Town Municipality.*[41]

2.2.2.3.1 Liability for negligence and the duty of care

Smillie (1982: 234) notes that the basic function of the tort of negligence is to shift accidental loss from the innocent victim to the person whose negligence caused the accident. Negligence is essentially the breach of a legal duty to take care resulting in damage caused and is defined by Baron Alderson in the famous English case of *Blyth v Birmingham Waterworks Company*[42] as follows:

> "Negligence is the omission to do something which a reasonable man, guided upon those considerations which ordinarily regulate the conduct of human affairs, would do, or doing something which a prudent and reasonable man would not do."

For a negligent action to hold the following must be established:

a) That the defendant owed the claimant a duty of care.
b) That the defendant broke the duty of care; that is a breach.
c) That the claimant suffered damage, to which the law affords compensation, as a result of the breach.

A professional person, such as an insurance intermediary, is especially exposed to liability from words, such as advice given. To the extent that this risk exists it cannot be to all persons. The first limitation will be to accept the risk is limited to Lord Atkin's neighbour principle. The principle of 'duty of care' was originally limited by applying Lord Atkin's 'neighbour test' which comes from *Donoghue v Stevenson*[43] a product's liability case:

[40] *Langley Fox Building Partnership (Pty) Ltd v De Valence* 1991 1 SA 1 A.
[41] *Butters v Cape Town Municipality* 1993 3 SA 521 C.
[42] *Blyth v Birmingham Waterworks Company* 1856 11 Ex Ch 781.
[43] *Donoghue v Stevenson* 1932 AC 562.

> "There must be, and is, some general conception of relations giving rise to a duty of care, of which the particular cases found in the books are but instances… The rule that you are to love your neighbour becomes in law you must not injure your neighbour; and the lawyer's question: 'Who is my neighbour?' receives a restricted reply. You must take reasonable care to avoid acts or omissions which you can reasonably foresee would be likely to injure your neighbour. Who, then, in law, is my neighbour? The answer seems to be – persons who are so closely and directly affected by my act that I ought reasonably to have them in contemplation as being so affected when I am directing my mind to the acts or omissions that are called in question"

Hedley Byrne & Co. Ltd. v Heller & Partners Ltd.[44] saw the House of Lords, in dealing with the question of if a defendant could be liable for pure economic loss as opposed to liability for damage to property or injury to people, recognized that a person making a statement could owe a duty of care to a recipient of that statement with whom he has no contractual relationship, and as such, in principle, he could be liable for pure economic loss. In short the defendant, a professional, could be liable for a negligent misstatement which causes a pure financial loss but limited to Lord Atkin's neighbours It was found that it is unacceptable to impose liability to all recipients of statements for financial losses they may suffer as a result of a negligent mis-statement; rather the liability had to be limited to cases where a 'special relationship' existed. This limitation was the application of Lord Atkin's neighbour test.

In *Caparo Industries plc v Dickman,*[45] another case involving pure economic loss and the duty of care, Lord Bridge stated that it:

> "is never sufficient to ask simply whether A owes B a duty of care. It is always necessary to determine the scope of the duty by reference to the kind of damage from which A must take care to save B harmless."

[44] *Hedley Byrne & Co. Ltd. V Heller and Partners Ltd*. 1964 A.C. 465.
[45] *Caparo Industries plc v Dickman*1990 2 A.C. 605 627.

In this case the House of Lords established a new three-stage test for the courts to consider regarding duty of care:

a) Were the consequences of the defendant's act reasonably foreseeable? An example of harm held to be reasonably foreseeable: *Jolley v Sutton LBC*[46].
b) Is there a legal relationship between the parties? An example of proximity in relationship: *Home Office v Dorset Yacht Club*[47].
c) If it would be fair, just, and reasonable for the law to impose a duty given the circumstances? An example of where the imposition of the duty was not fair is seen in *Hill v Chief Constable of West Yorkshire*[48].

"The emergence of the *Caparo* approach as the prevailing basis upon which to determine the duty question, means that considerations of fairness, justice and reasonableness now play a central role as the cutting edge of negligence. In considering this, the courts take into account both broad issues of policy, and any effects which might be generated by the imposition of a duty of care" (Hartshorne, Smith, Everton; 2000: 504).

The application of the criteria for the duty of care laid down in the *Caparo* case is evident in the case of *South Australian Asset Management v York Montagu Ltd*.[49]. This case involved the negligent valuation of a property by the defendant to a lender; the property was offered by a third party as security for a loan. The valuation of the property was one of the factors that affected the lenders decision to lend, as well as the terms of the loan, and as such, the House of Lords held that the valuer should be held only partly liable. A distinction was drawn between a professional who provided information, the role of the valuer in this case, and a professional who actually advised a client whether to enter or not to enter the transaction (Clarke; 2000).

The position of insurance brokers with regard to duty of care was considered in *Aneco Reinsurance Underwriting Ltd. V Johnson & Higgins Ltd*. 2000 1 All E.R. (Comm.) 129; this

[46] *Jolley v Sutton LBC* 2000 1 WLR 1082.
[47] *Home Office v Dorset Yacht Club* 1970 AC 1004.
[48] *Hill v Chief Constable of West. Yorkshire* 1989 AC 53.
[49] *South Australian Asset Management v York Montagu Ltd*. 1997 1 A.C. 191.

case is discussed in further detail in Section 5.1. In sharp contrast to the *South Australian* case, the Court in *Aneco* held the brokers fully liable with Aldous L.J. stating that:

> "to hold [the brokers] responsible for the full loss that has arisen does not impose upon them a liability greater than they could reasonably have thought they were undertaking."

Clarke (2000) notes that as the brokers were acting not only for Aneco but also for the Lloyd's underwriters, it is difficult to see how, as the House of Lords in the *South Australian* case seemed to insist, the brokers were advising Aneco whether or not to enter the relevant transaction, i.e. the reinsurance of the Lloyd's underwriters; they could not do so for one party and not the other or even both.

2.2.2.4 Causation

For liability to attach in delict a person must *cause* damage. In Roman law cause meant that a positive act by one person would cause tangible harm to the person or property of another or would cause the prohibited consequence.

In modern law a causal link must exist (in law) between the conduct and the damage for liability to attach in delict. There are two types of causation (factual and legal) and both must be proven for causation to exist.

The courts have found that the *conditio sine qua non* test, or the 'but for' test, to be a convenient test to determine whether a causal link exists. This test is formulated as follows: but for the conduct of the defendant, would the harm have occurred? It is further explained in *International Shipping Co (Pty) Ltd v Bentley*:[50]

> "The first [enquiry] is a factual one and relates to the question whether the defendant's wrongful act was a cause of the plaintiff's loss. This has been referred to as 'factual

[50] *International Shipping Co (Pty) Ltd v Bentley* 1990 1 SA 680 (A) 700.

> causation'. The enquiry is generally conducted by applying the so-called 'but-for' test, which is designed to determine whether a postulated cause can be identified as a *causa sine qua non* of the loss in question. In order to apply this test one must make a hypothetical enquiry as to what probably would have happened but for the wrongful conduct of the defendant. This enquiry may involve the elimination of the wrongful conduct and the substitution of a hypothetical course of lawful conduct and the posing of the question as to whether upon such an hypothesis plaintiff's loss would have ensued or not. If it would in any event have ensued, then the wrongful conduct was not a cause of the plaintiff's loss; *aliter*, if it would not so have ensued. If the wrongful act is shown in this way not to be a *causa sine qua non* of the loss suffered, then no legal liability can arise."

Causation by omission (*conditio cum qua non*) requires a hypothetical addition to the scenario: if a person did what they were supposed to do, would the prohibited consequence have been avoided?

Thus factual causation, especially when applied to omissions can expose possible defendants to a limitless number of claims that emanate from his conduct; to restrict this limitless liability, legal causation is used.

Up until 1990 the law adopted various specific tests of legal causation, specifically, the Test of Adequate Causation, the *nova causa interveniens* Test, the Individualisation Tests, and the Foresee Ability Theory. However the effect of the judgment in *S v Mokgethi*[51] was to demote these specific tests to merely being factors of consideration. The ultimate test is now the Mokgethi's sufficiently close connection test which poses the question of whether there is a sufficiently close connection between the conduct of the accused and the prohibited consequence.

[51] *S v Mokgethi* 1990 1 SA 32 (A) 39.

2.2.2.5 Damage

In Roman-Dutch law damage meant damage to corporeal property and caused by an external act, for example wounding a horse. This was later extended by the courts to include other forms of damage.

With regard to modern law, Neethling *et al* (2006:196) define damage as the detrimental impact upon any patrimonial or personality interest deemed worthy of protection by the law. Damage includes patrimonial (pecuniary) as well as non-patrimonial (non-pecuniary) loss. Pecuniary losses in so far as persons are concerned include medical and other expenses, loss of earnings, and loss of support, and non-pecuniary losses include general damages including pain, suffering, bodily disfigurement, and loss of life expectancy.

Historically damage meant damage to corporeal property and injury to people but more recently the question of whether damage included instances when there is no physical damage to property or injury to people has come to the fore. These are losses which are of a purely financial nature or as is often said, pure economic losses, and even earlier referred to a 'mere pecuniary loss'. This issue has been the subject of extensive debates. "Pecuniary loss is regarded on an entirely different footing from physical harm. The phrase 'mere pecuniary loss' describes a claim for damages that is unconnected with any physical harm whatsoever, for instance, a claim against an attorney, who negligently failed to have a will properly attested, that one has lost a legacy" (Tager, 1973: 297).

2.2.2.5.1 Liability for pure economic loss

It should be clear that in most cases involving an insurance intermediary, the loss suffered by the third party will be pure economic in nature and not physical injury (*Delphisure Group Insurance Brokers Cape (Pty) Ltd v Dippenaar and others*).[52] The issue of liability for pure economic losses is thus of paramount importance when investigating the legal liability of insurance intermediaries.

[52] *Delphisure Group Insurance Brokers Cape (Pty) Ltd v Dippenaar and others* 2010 5 SA 499 SCA.

Bussani, Palmer and Parisi (2003: 115) note that the historical and comparative study of civil law economic rules reveals that there has never been a universally accepted definition of what constitutes 'pure economic loss'. Neethling *et al* (2006) however provide a description of 'pure economic loss' to comprise patrimonial loss that does not result from damage to property or injury to people or financial loss that results from damage to property or impairment to personality but which does not involve the plaintiff's property or person. This is as opposed to consequential economic loss which, as noted by Brown, Neyers and Pitel (2005), is a financial loss relating to some physical damage to a person or property. Smillie (1982) notes that there is a legal requirement of actual physical damage in cases concerning consequential economic loss, which effectively limits the number of claims, making it more predictable than pure economic losses.

Stuhmcke (2001: 18) notes that historically compensation has not been recoverable where only pure economic loss has occurred. Delictual liability where the damage is of a purely economic nature varies throughout in the world. Parisi, Palmer and Bussani (2007: 29-30) note that a rule of no-recovery in tort for pure economic loss is closely identified with conservative regimes such as Germany, Austria, Portugal and the Scandinavian systems, but in liberal regimes such as France and Belgium no such rule appears to exist.

Liabilities arising from damages that are of a pure economic nature are a pertinent issue when considering intermediaries: when an intermediary is sued the damage involved will almost always be pure economic in nature. A review how different jurisdictions treat claims for pure economic losses is now undertaken.

- United Kingdom

English law, as opposed to some other legal systems, considers pure economic loss as being part of the law of contract; only in exceptional circumstances will pure economic loss be recoverable in tort (Banakas; 1996).

The rule of no liability in negligence for pure economic losses was firmly established in England in the case of *Cattle v Stockton Waterworks Co*.;[53] here the court held that since no harm was intended there should be no liability. Because a single incident may cause foreseeable economic loss of vast amount to a very large number of persons, it was felt that to allow victims of purely economic loss to recover in a negligence action by application of normal principles would impose a burden of liability on defendants out of all proportion to their culpability, result in unwarranted curtailment of productive activity, and lead to a multiplicity of litigation arising out of a single event which could present serious administrative problems for the courts (Smillie; 1982: 231).

In *Derry v Peek*[54] the plaintiffs brought an action in deceit against the directors of the company for false statements in the company prospectus upon which the plaintiffs had relied to invest in the company. As noted by Feldthusen (1994), the court held that the directors honestly believed that the statements were true, but had no reasonable grounds for believing so; the Court of Appeal held that the defendants had established fraud at law on this basis, however the House of Lords disagreed. Lord Hershell stated that:

> "First, in order to sustain an action of deceit, there must be proof of fraud, and nothing short of that will suffice. Secondly, fraud is proved when it is shown that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, careless whether it be true or false."

Three quarters of a century later the decision of the House of Lords in *Hedley Byrne & Co. Ltd. v Heller & Partners Ltd.*[55] however effectively reversed the result of *Derry v Peek*[56]and established that "negligent misstatements causing pure economic losses to a plaintiff who had no relevant contractual rights become recoverable" (Banakas; 1996: 29). Liability under the *Hedley Bryne* rule was however still subject to some conditions. Smillie (1982: 232) notes that the House of Lords recognized liability in tort for negligent statements causing pure economic losses

[53] *Cattle v Stockton Waterworks Co*. 1875 L.R. 10 Q.B. 453.
[54] *Derry v Peek* 1889 14 App Cas 337.
[55] *Hedley Byrne & Co. Ltd. v Heller & Partners Ltd.* 1964 A.C. 465.
[56] *Derry v Peek* 1889 14 App Cas 337.

where there is a 'special relationship' between the parties in the case of *Hedley Byrne & Co. Ltd. v Heller and Partners Ltd.*[57] and states that "since *Hedley Byrne*, the exclusionary rule [of no liability] has been subject to repeated challenge in cases of purely economic loss caused by negligent acts and omissions, rather than statements". Their Lordships recognized that a person may be under a duty to act carefully with respect to the financial interests of another person not only as a result of contractual agreement but also in certain 'special relationships' such as fiduciary obligations (Gosnell; 2000: 138).

The English Court of Appeal then denied the recovery for pure economic loss thereby affirming the no liability rule in the case of *Spartan Steel & Alloys Ltd. v Martin & Co. (Contractors) Ltd.*[58] Marshall (1975: 750) notes that six of the principle justifications for the English refusal to extend liability for pure economic loss into a general principle are:

1) The danger of multiplicity of claims, which would be (a) vexatious to the court and (b) unfair to the defendant who may merely have made an inadvertent slip completely out of proportion with the wide extent of the economic consequences.
2) The overwhelming amount of damages for which the defendant might be liable.
3) The fear of stifling commerce and enterprise.
4) What is involved is often loss of profits, i.e., *lucrum cessans* rather than *damnum emergens*, and the former should not have as high a priority in recovery as the latter.
5) Economic loss is a less important interest than physical damage.
6) The danger of fictitious claims.

Tager (1973: 297-298) concurs that claims for mere pecuniary loss are usually refused on the ground that to allow them would result in a multiplicity of actions.

The influence of the judge Lord Denning however saw the liability for economic loss being recognized in *Anns v Merton London Borough Council*.[59]. This case did not directly deal with the issue of pure economic loss but rather physical damage caused by negligence. It was from

[57] *Hedley Byrne & Co. Ltd. V Heller and Partners Ltd*. 1964 A.C. 465.
[58] *Spartan Steel & Alloys Ltd. v Martin & Co. (Contractors) Ltd.* 1973 Q.B. 27.

[59] *Anns v Merton London Borough Council* 1978 AC 728 HL.

this case that the '*Anns* Test' developed; this test measured the duty of care for negligent acts, including pure economic loss. McInnes (1993: 12) notes that from the dictum of Lord Wilberforce, recovery should depend on the following two criteria:

i. Sufficient proximity between the parties such that the defendant could reasonably foresee that carelessness on his part would cause damage to the plaintiff; and
ii. The absence of considerations calling for a limitation on liability, including those relating to the nature of the damage sustained.

Junior Books Ltd. v Veitchi Co. Ltd.[60] then saw recoverability for foreseeable economic losses being extended to cover any situation in which the defendant may foresee that another might suffer an economic loss. Here the House of Lords found that the *Anns* Test could be equally applicable to cases involving economic losses. Prior to this decision the generally accepted doctrine was that a plaintiff who was caused economic loss by a defendant's wrongful act, whether it was a breach of contract or tort, against a third party, could not maintain an action; Fridman (1990) notes that this case appeared to push the limits too far and that the decision was based upon and should have been restricted solely to its own special facts.

However in the subsequent case of *Murphy v Brentwood District Council*[61] the House of Lords unanimously overturned its previous decisions and rejected any general doctrine which would recognize liability for economic loss. The reason for rejecting a general doctrine for liability for pure economic loss is the failure to define a legal basis of such liability. In the absence of a clear legal basis liability exists purely at the arbitrary discretion of the judge. Feldthusen (1994) notes that the exclusionary rule, consistent with the *Murphy* philosophy, has been solidified in recent cases: *Leigh & Sillivan v Aliakon Shipping Co.*[62] and *Candlewood Navigation Corp. v Mitsui O.S.K. Lines Ltd.*[63] Tan (1995: 194) also suggests that "it is practically unarguable, in the English context, that pure economic loss is recoverable. The decision in *Murphy* is quite unequivocal, at least in spirit, that pure economic loss is irrecoverable".

[60] *Junior Books Ltd. v Veitchi Co. Ltd.* 1982 3 All ER 201.
[61] *Murphy v Brentwood District Council* 1990 2 All ER 908 HL.
[62] *Leigh & Sillivan v Aliakon Shipping Co.* 1986 2 All E.R. 145 (H.L.).
[63] *Candlewood Navigation Corp. v Mitsui O.S.K. Lines Ltd.* 1985 2 All E.R. 935 (P.C.).

Subsequent to the *Murphy* judgment in *Spring v Guardian Assurance*[64] the House of Lords addressed the issues of negligence and pure economic loss and held that an employer owed a former employee a duty to prepare a reference with reasonable care. Banakas (1996) notes that the *Spring* case represents a major extension of *Hedley Bryne*. The trial judge had found that the plaintiff owed a duty of care and ordered for damages to be assessed, however the Court of Appeal reversed the decision holding that the plaintiff's only remedy lay in defamation, in which no action could succeed.

- Malaysia

The High Court of Malaysia gave its approval to the House of Lords decision in the *Murphy* case with judge Wan Mohammed H, in the case of *Government of Malaysia v Cheah Foong Chiew and Ors*[65], stating that the decision of the *Murphy* case was satisfactory and appropriate.

- Australia

A challenge to the exclusionary rule came from the High Court of Australia in *Caltex Oil (Australia) Pty. Ltd. v The Dredge 'Willemstad'*.[66] The High Court refused to accept any general rule against recovery of economic loss. Here the court sought to enforce a new general application that allowed for recovery where the defendant "knew or ought to have known that the plaintiff as a 'specific individual' was likely to suffer economic loss" (Smillie, 1982: 233). The need to limit the availability of pure economic loss was highlighted by Hayne J in this case:

> "So that commerce, providers of services, courts and society generally will not have to bear the burden and uncertainty of incalculable claims by a mass of people whose identity or very existence may be unknown to the defendant."

[64] *Spring v Guardian Assurance* 1994 3 WLR 354.
[65] *Government of Malaysia v Cheah Foong Chiew and Ors* 1993 2 M.L.J. 439.
[66] *Caltex Oil (Australia) Pty. Ltd. v The Dredge 'Willemstad'* 1976 136 C.L.R. 529.

More recently in the case of *Cattanach v Melchior*[67] the High Court dealt with the issue of pure economic loss with regard to medical negligence, a case of the so-called doctrine of wrongful birth. Here a couple became the parents of an unintended child as a result of medical negligence and claimed damages from the doctor of the cost of raising and maintaining the child. It was held that the loss was compensable.

Torre and Clifford (2005: 161) note that in contemporary Australia, where the injurer does some act and causes the victim pure economic loss, the heuristics, which will be used by the High Court in assessing whether there is a duty of care to avoid causing such a loss, are reasonable foreseeability of injury; proximity and the cost effectiveness of injurer and victim self-protection.

- Canada

During the 1980's and 1990's the Supreme Court of Canada began to move away from the exclusionary rule and started imposing liability for pure economic losses in certain instances. Feldthusen (1994: 4, 317) notes that the decision of *Murphy v Brentwood District Council*[68] has not been well-received in Canada "but the state of law there defies general summary"; however the Supreme Court's decision in *Rivtow Marine Ltd. v Washington Iron Works*[69] is to the same effect as that of *Murphy*, implying the acceptance of the exclusionary rule.

More recently, the case of *Martel Building Ltd. v Canada*[70] indicates the current position held in Canada. Here the Court of Appeal held that a duty of care had been breached and that a causal link existed between the respondent's loss and the appellant's negligence. Even though it was acknowledged that at common law recovery of economic loss was not allowed where no physical harm or damage to property had been suffered, the law now recognized five categories of compensable economic loss. According to Brown et al (2005: 88) the five categories into which pure economic loss could be separated are as follows: (a) the independent liability of statutory

[67] *Cattanach v Melchior* 2003 HCA 38.
[68] *Murphy v Brentwood District Council* 1990 2 All ER 908 HL.
[69] *Rivtow Marine Ltd. v Washington Iron Works* 1974 S.C.R. 1189.
[70] *Martel Building Ltd. v Canada* 2000 2 S.C.R. 860.

public authorities, (b) negligent misrepresentation, (c) negligent performance of a service, (d) relational economic loss, and (e) negligent supply of shoddy goods or structures.

- United States

In discyssing delict (torts in the U.S.) in the U.S. it must be kept in mind that tort is a state not federal matter. Thus essentially each state is different and to understand the developments in the U.S. is equivalent to 52 separate countries not a single unified company. Feinman (2006) notes that the first major accountant liability decision, which by nature involved a claim for pure economic loss, in the United States became worldwide the leading decision in the entire field of third party liability for economic loss, that of *Ultramares Corp. v Touche.*[71] This case is still quoted routinely in judgemenrs on the topic. However, prior to this case the New York court had decided on two other important third party cases.

In *MacPherson v Buick Co.*[72] the court used the rule in *Winterbottom v Wright*[73] of contractual privity as the liability standard for actions by third parties for personal injury. Following this, the court imposed liability for economic loss for third party beneficiary recovery in *Glanzer v. Shepard.*[74]

In the *Ultramares* case it was held that the accountants should not be held liable by third parties for negligence; thus the court refused to extend the foreseeability principle of the *MacPherson* case to economic losses as a result of an accountant's negligence.

In the famous words of Judge Cardozo in the *Ultramares* case:

> "If liability for negligence exists, a thoughtless slip or blunder, the failure to detect a theft or forgery beneath the cover of deceptive entries, may expose accountants to a liability in an indeterminate amount for an indeterminate time to an indeterminate class."

[71] *Ultramares Corp. v Touche 1931* 255 NY 170.
[72] *MacPherson v Buick Co.* 1916 111 N.E. 1050.
[73] *Winterbottom v Wright* 1842 152 Eng. Rep. 402.
[74] *Glanzer v. Shepard* 1922 135 N.E. 275.

Van Boom, Koziol and Witting (2004) suggest that Cardozo's words imply that a court must consider all the possible consequences of allowing a claim regardless of what the claim is in respect of and if the foreseeable result is indeterminacy then the court should dismiss the claim.

Rizzo (1982) notes that the decision in *Ultramares* is clearly inconsistent with the decision in *Glanzer*; where both cases dealt with economic loss negligently caused, recovery was denied in the former but allowed in the latter.

Atiyah (1985) notes that claims for economic loss, as characterized by English courts, are referred to as 'negligent interference with contractual relations' in the United States. In the United States the general principle is of no recovery for negligent interference with contractual relations.

Banakas (1996) notes that in the United States the common law of economic loss is much the same as that in the Commonwealth. "Because the American legal system includes numerous distinct jurisdictions for private law, it is difficult to name with certainty the policies that are crucial in deciding cases of economic loss arising from negligence. Although all states generally apply the economic loss rule, they do not all do so for the same reasons. In some cases, the states appear split on whether to apply the rule at all in a particular context" (Gruning; 2006: 206).

- South Africa

In South African case law the case of *Cape of Good Hope Bank v Fischer*[75] was the first to deal with damages of a purely economic nature in which the court implied that the *Lex Aquilia* as extended was broad enough to cover claims for pure economic losses with De Villiers CJ commenting that:

> "the *Aquilian* law had received an extension by analogy to an extent never permitted under the Roman law. The action *in factum* was no longer confined to cases of damage

[75] *Cape of Good Hope Bank v Fischer* 1886 4 SC 368.

> done to corporeal property, but was extended to every kind of loss sustained by a person in consequence of the wrongful acts of another and, thus extended, bore a curious analogy to the action on the case in the English law."

However, historically liability for pure economic loss was not known in both the Roman and Roman-Dutch common laws. As stated in the Institutes of Justinian by Moyle (1913: 169): If damage be done, not by the body or to the body, but in some other form, neither the direct nor the modified Aquilian action will lie, though it is held that the wrongdoer is liable to an action on the case. This action however should not be considered as a remedy; an action is nothing else than the right of suing before a judge for what is due to one (Moyle; 1913: 173). No authority has ever been found in Roman law for liability attaching to pure economic loss.

Van Aswegan (1996: 566) summarized the position of the *Fischer* case as follows:

> "the sentiments articulated in the first case [*Cape of Good Hope Bank v Fischer*] did not accurately reflect the development of South African law at that stage. While it is true that the area of application of the *action legis Aquiliae* has been extended significantly through the years, especially in regard to liability for omissions, negligent misrepresentations, and pure economic loss, this development came at a much later stage. The statement in the *Fischer* case can thus be regarded as best as a somewhat optimistic prediction of the future development of the action in South African law".

By the twentieth century South African courts began to accept a general doctrine that all damages which are caused intentionally or negligently are actionable. As noted by Hutchison (1996: 595) the development of liability for omissions, negligent misstatements and pure economic loss was made possible by the "resurrection and redefinition of the element of wrongfulness, which has come to serve a very prominent role as a discretionary tool for judicial control in expanding the frontiers of Aquilian liability."

The case of *Perlman v Zoutendyk*[76] saw the court holding on an exception that the *LexAquilia* as extended does cover liability for economic losses. Watermeyer J provided a rather broad description of liability by stating that:

> "… in general all damage caused unjustifiably (*injuria*) is actionable, whether caused intentionally (*dolo*) or by negligence (*culpa*)."

The decision of the *Perlman* case was highly controversial. McKerron (1973: 90), who was the leading authority on this area of law at the time, noted, decades later, that it was probably no exaggeration to say that the leading heresy in the law of delict is the view expressed by Watermeyer J in *Perlman v Zoutendyk*[77] that the *Aquilian* action affords a general remedy not only for physical injury to person or property but also for mere pecuniary or economic loss.

Delictual liability for economic loss caused by negligent misstatement remained, for a long time, unclear in South Africa. In the first appeal court *Herschel v Mrupe*[78] the Appellate Division was reluctant to recognise liability for economic loss caused by negligent misrepresentation; this was due to the influence of English law which only recognised liability for intentional misrepresentation.[79]

Liability for pure economic loss was finally introduced in the High Courts (known at the time as the Supreme Courts) in *SA Bantoetrust v Ross en Jacobz.*[80] After this it was a matter of time before the matter would go back to the Appellate Division, which it did in the case of *Administrateur Natal v Trust Bank van Afrika Bpk*[81] which saw Chief Justice Rumpff confirm the introduction of liability for economic loss; he was critical of the *Bantoetrust* case, feeling constrained to introduce this form of damage but promised that the court would keep this form of liability under strict control. After the recognition in *Administrateur Natal* a large and increasing number of cases have been dealt with by the courts which involved pure economic losses.

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[76] *Perlman v Zoutendyk* 1934 CPD 151 155.
[77] *Perlman v Zoutendyk* 1934 CPD 151 155.
[78] *Herschel v Mrupe* 1954 (3) SA 464.
[79] As seen in *Derry v Peek* 1889 14 AC 337.
[80] *SA Bantoetrust v Ross en Jacobz* 1977 3 SA 184 T.
[81] *Administrateur Natal v Trust Bank van Afrika Bpk* 1979 3 SA 824 A.

The application of the doctrine of liability for pure economic loss was summarized in *Lillicrap, Wassenaar & Partners v Pilkington Bros (SA) (Pty.) Ltd.*[82] by Grosskopf JA:

> "It is clear that in our law Aquilian liability has long outgrown its earlier limitation to damages arising from physical damage or personal injury. Thus, for instance, in *Administrateur, Natal v Trust Bank van Afrika Bpk* 1979 (3) SA 824 (A) this Court held that Aquilian liability could in principle arise from negligent misstatements which caused pure financial loss, i.e. loss which was caused without the interposition of a physical lesion or injury to a person or corporeal property."

This case is significant for another reason; concurrent liability. The court ruled that if the parties were bound by contract, the dispute must be resolved in contract not delict. In 1991 the Appellate Division found that there is a legal duty on the parties engaged in pre-contractual negotiations to not make misstatements in; the breach of such a duty may give rise to a delictual claim for damages for pure economic loss caused by misstatement.[83]

A number of cases involved both delict and contract and without any comment the courts accepted the action could be brought in either delict or contract. An example of this was the case of *Durr v Absa*[84] which is of particular interest to intermediaries, since it involves liability for giving investment advice, a common activity of some intermediaries. This case involved a claim for pure economic loss arising out of investment advice which having been accepted and acted on, lost money. The court held that the Absa branch manager was negligent in performing his duty and as such, ABSA was vicariously liable for the actions of the employee. Without any reference to the problem of concurrent liability and the ruling in the *Pilkington* case *supra*, the court decided this case in delict and not contract. It was almost as if the court was unaware of the *Pilkington* ruling. Of course if the court can decide contractual matters in delict, this spells the death of contract as discussed herein.

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[82] *Lillicrap, Wassenaar & Partners v Pilkington Bros (SA) (Pty.) Ltd.* 1985 (1) SA 475 (A).
[83] *Bayer South Africa (Pty.) Ltd. v Frost* 1991 (4) SA 559 (A).
[84] *Durr v Absa Bank Ltd* 1997 3 SA 448 SCA.

Since its recognition in the *Trust Bank* case, liability for pure economic loss had featured in a very large number of cases, including against insurance brokers and agents. Delictual liability for pure economic loss in South African law is based on the normal principles of delict and requires an act of commission or omission, factual and legal causation, damage in the form of pure economic loss, fault (negligence or intent), and wrongfulness (Palmer and Bussani; 2008: 220). However, despite thousands of cases involving the concept of wrongfulness it was recently admitted that this concept lacks legal clarity.[85] The reservations expressed by McKerron (1973) and in essence unanimously endorsed by the House of Lords in the *Murphy* case is as valid as when made by McKerron in 1973. The fundamental basis of liability for pure economic loss cannot, as a point of law, be determined.

It is thus accepted that liability for pure economic loss does indeed exist in modern South African case law; liability however if found in specific cases, rests more on the opinion of the court than objective law. Thus it would seem that liability is no longer a point of fact and law,[86] but largely a point of judicial opinion.

2.2.3 Concurrency of actions and the death of contract

Maine's (1861) famous dictum suggests that the movement of progressive societies has been from status to contract.

[85] Fagan (2005) suggests that the standard academic view of wrongfulness (i.e. a harm-causing act was wrongful if, and only if, it was unreasonable, that being judged from an ex post facto perspective) that is accepted by South African delict scholars is mistaken and that the Supreme Court of Appeal has recognised a 'general test' for wrongfulness in the law of delict which does not vindicate the standard view. Furthermore Fagan (2005) notes that wrongfulness is determined in part by judicial discretion which may effectively change the rules that are to be applied to determine wrongfulness in the future. Neethling (2006) suggests that there is an overlap between negligence and wrongfulness with the test for negligence being used to determine wrongfulness. Paizes (2008: 371) further suggests that the treatment of wrongfulness by the law is confusing, unclear, contradictory and vague. Paizes (2008) attributes the difficulty of making sense of wrongfulness to the following, amongst other things: an inconsistency in the meaning of wrongfulness both in different areas of law and within the same area of law, a blurred distinction between wrongfulness and fault, and the relationship between wrongfulness and causation.

[86] As suggested by Fitzgerald (1966: 65-66) all questions which arise for consideration in a court are either questions of law or questions of fact. A question of fact is all questions which are not authoritatively answered by the law; a fact being everything that is not law. A question of law is a question which a court is bound to answer in accordance with the rule of law, excluding the right of the court to answer a question as it thinks fit in accordance to what is considered to be truth and justice of the matter.

Cohen (1933: 553, 558) notes that Maine's (1861) observation of the progress of law suggests that a legal system where "rights and duties are determined by agreement of the parties is preferable to a system wherein they are determined by 'status'"; this progression is partly true only within certain periods of expanding trade and that "in the wake of increased freedom of contract we find increased regulation, either through the growth of custom and standardization or through direct legislation".

Wilson (1993: 282) affirms that Maine's (1861) observation implies that "where social relations had once been understood as depending on who you were (your status), they were increasingly determined by what you did, that is, by the legal relationships you voluntarily entered into" but that this notion of a shift from status to contract has been challenged by *Slade's Case*.[87] Soifer (1987: 1929) also suggests that "*Betty's Case* and the role of the law during Reconstruction and its aftermath together challenged Sir Henry Maine's claim" of the movement of law.

"The law of England is to be found in judicial decisions and partly in Acts of Parliament… Most of our fundamental legal principles have emerged from decided cases. In principle it is much more straightforward to take your law from a statute, where you will, if you are lucky, find statements of law laid down in simple language, uncluttered by the detailed facts of particular cases" (Diamond; 1968: 361).

By the mid-nineteenth century the boundary between contract and tort was to be, as noted by Ogilvie (1984: 199), the distinction between obligations which are voluntarily assumed and obligations which are imposed by law. However the distinction between contract and delict has become considerably blurred in modern law due to the fact that modern legal systems have addressed issues dealing with the expansion of liability in varying ways.

Zimmermann (1990: 903) makes the following contrast between contract and delict:

> "…a delict is a civil wrong. Yet breach of contract, in a broad sense, may also be dubbed a civil wrong. Within the province of private law, the necessity of drawing a second distinction thus presents itself. Ever since the days of Gaius,

[87] *Slade's Case* 1602 4 Co. Rep.

> Civilian tradition has conceived of contract and delict as two separate branches of the law of obligations, and in the English common law, too, a very similar conceptual classification (contract and tort) has been firmly entrenched. It has already been mentioned repeatedly that the distinction between delict (or tort) and contract is a most delicate one and that the borderline has in many respects become blurred. What is regarded as contractual liability in one country may be added to the province of delict in another, and *vice versa*, and certain cases even appear to defy all attempts at classification: being in the nature of hermaphrodites, they lead an unsettled existence within the no man's land somewhere between the traditional and established categories".

O'Connell (1977: 673) suggests that, like labour law, insurance law is a field wherein contract is dead and that the courts will apply tort criteria when deciding who is to bear the loss if a contract falls apart and notes that this raises a profound contradiction: "How can the courts use contract doctrines to impose tort liability if they are using tort doctrines to impose contract liability?". Moreover O'Connell (1977: 675, 676) notes that the American government will not favour contracts where "potential accident victims have waived their tort remedies" but suggests that the reason why the waiver of these rights might be approved by courts whereas "other contracts stripping potential victims of their tort rights would not, is that workers' compensation benefits provide a compensatory base". O'Connell (1977: 683) further suggests that contract law can only be used in place of tort liability where "guarantees of substantial payment supplant the vicissitudes of traditional tort liability".

Esser (1996: 624) concurs that the classical distinction between contract law and tort law is decaying and notes that the distinction between "contractual relations and tort relations in terms of whether the civil liability arose out of the explicit agreement between the parties to a given transaction or out of a general obligation of one party toward another arising out of their ongoing social relationship" no longer exists.

Scott (2004: 369) notes that "[Gilmore (1974)] saw the expansion of legal liability for relied-upon promises as evidence that contract was being swallowed up by tort and would soon disappear as an independent, coherent body of law".

South African courts have experienced a shift in their approach to the problem of the concurrency of action of contract and delict. Although contractual and delictual liability have never traditionally been considered as exclusive of each other, the decision in *Lillicrap, Wassenaar and Partners v Pilkington Brothers (SA) (Pty) Ltd.*[88] brought on an important qualification to this principle. In this case Grasskopf AJA implies that "a concurrence of delictual and contractual liability is no longer permissible where the harm does not flow from physical damage to the person or to a specific piece of property of the plaintiff, but where it is of a purely economic nature" (Zimmermann; 1990: 906) by stating that:

> "the Aquilian action does not fit comfortably in a contractual setting like the present."

However, the *Lillicrap* case is not authority for the more general issue of whether an action cannot be brought in delict if there already stands a valid contractual claim. Grosskopf AJA emphasized the fact that South African law does acknowledge a concurrency of actions where the same claim can give rise to damages both in delict and contract, and furthermore allows the plaintiff to chose which action he wishes to use. The problem created by the expansion of delict is seen in *Durr v Absa Bank Ltd.*[89] where the broker, Absa, was held liable in delict for the damages suffered by an investor, Durr, who was negligently advised; here Schutz JA, without giving any specific consideration to the problem of concurrent actions stated that:

> "the claim pleaded relied upon contract, alternatively delict, but as the case was presented as one in delict, and as nothing turns upon the precise cause of action, I shall treat it as such."

The court in the *Durr* case effectively disregarded the decision of *Lillicrap* which stated that where the relationship of the parties was governed by contract, the action should be brought in contract rather than delict if there exists a concurrency of action.

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[88] *Lillicrap, Wassenaar and Partners v Pilkington Brothers (SA) (Pty) Ltd* 1985 1 SA 475 (A) 500 503-504.
[89] *Durr v Absa Bank Ltd* 1997 3 SA 448 SCA.

Henderson v Merrett Syndicates Ltd.[90] was a landmark case in which the House of Lords established the possibility of concurrent liability in both tort and contract; the claims were allowed to be made in both tort and contract which blurred the divide between the two. By allowing this action the House of Lords overruled Lord Scarman's ruling in *Tai Hing Cotton Mill Ltd. v Liu Chong Hing Bank Ltd.*[91] which held that:

> "there is nothing advantageous to the law's development in searching for liability in tort where the parties are in a contractual relationship."

Scott (2004) suggests that contract can be revived if the courts can see that less contract law is better than more. O'Connell (1977: 685) however suggests that the issue is not so much the death of contract or the death of tort but rather what is needed is "the orderly, if admittedly imperfect, justice of no-fault insurance, with its mixture of contract and tort".

What has emerged as a result of this mixture between contract and tort is known as 'quasi-contract'; this was however not part of the nineteenth century theory of contract. Gilmore (1974: 88) notes that quasi-contract is thought of as "a sort of no-man's-land lying between contract and tort. In the early part of the century the concept served to blur the sharp edges both of contract theory and tort theory. It was, as the courts readily admitted, a legal fiction".

2.3 Statute

"The condition of its statute laws must always be a matter of very great interest and importance to any political community. It is clearly to the advantage of the State that its individual members should be well acquainted with the laws by which they are governed and whose operation affects to a greater or less extent their conduct and business and their relations with one another" (Carrington; 1890: 225).

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[90] *Henderson v Merrett Syndicates Ltd.* 1995 2 AC 145.
[91] *Tai Hing Cotton Mill Ltd. v Liu Chong Hing Bank Ltd*. 1986.

In addition to the common law the other body of law that exists is statute law. Atiyah (1985: 2) notes that when a statute is passed it becomes part of the law, similar to a new case, and that it essentially modifies or reverses the existing law; "a statute is law, and *prima facie* matters of law fall within the jurisdiction of the courts".

Carter (2010) notes that matters which are not specifically governed by the insurance legislation will be governed by the general principles of South African law such as contract and delict (as previously discussed).

Short-term insurance is increasingly heavily regulated in South Africa and insurance intermediaries must comply with the following legislation: Financial Advisory Intermediary Service Act 37 of 2002, Short-Term Insurance Act 53 of 1998, Financial Services Ombud Schemes Act 37 of 2004, and Policy Holder Protection Rules (Long and Short-Term Insurance) 2004.

2.3.1 FAIS

The Ministry of Finance of South Africa has explored various mechanisms for the regulation of market conduct within the financial services industry since 1993, the intention being to protect consumers and enhance the integrity of the financial services industry. This was achieved by the enactment of FAIS in November 2002.

The Financial Advisory and Intermediary Services Act (FAIS) was brought about to regulate the financial services industry by the Financial Services Board (FSB). FAIS is essentially responsible for the regulation of giving advice and the activities of intermediaries, which was a previously unregulated activity. It requires that financial services providers be licenced and authorised through the FSB. The Act is in addition to any other existing laws that are not inconsistent with its provisions and does not replace any such laws.

FAIS not only applies to people in the insurance industry but also to all financial entities that provide a financial product, such as banks. Any person who provides advice on intermediary

services as defined by the Act is subject to the Act and its regulations. The Act seeks to ensure that clients are protected from improper conduct by financial services providers and are treated with due skill, integrity and diligence in respect of the giving of advice and the provision of intermediary services, such as the processing of insurance claims.

Bracher (2010) notes that the basis of an intermediary's liability is better understood since the enactment of FAIS; this essentially means that the number of claims against intermediaries has increased.

FAIS consists of seven chapters, each chapter covering key provisions:

	Chapter	*Description*
Introduction	Definitions and applications	• Defines key terms • Explains scope of application
Chapter 1	Administration of FAIS	• Explains the establishment of the Registrar for financial service providers and describes its powers • Explains the establishment of the Advisory Committee of financial service providers
Chapter 2	Authorisation of financial service providers	• Explains how to apply for a financial service providers licence, and the conditions for suspension or withdrawal of licences • Explains the conditions necessary to permit exemptions from FAIS
Chapter 3	Representatives of financial service providers	• Outlines the requirements for qualifications of representatives and key individuals • Specifies the conditions for debarment of representatives and key individuals • Describes the duties of a financial service provider
Chapter 4	Codes of conduct	• Explains the codes of conduct applicable to all financial service providers, key individuals, and representatives

Chapter		*Description*
Chapter 5	Duties of financial service providers	• Details the requirements for appointing a compliance officer • Stipulates audit requirements for financial service providers
Chapter 6	Enforcement	• Establishes the office of the Ombudsman for financial service providers and explains their duties • Civil remedies • Specifies offences, fines, and penalties
Chapter 7	Miscellaneous	• Protects rights of person to seek redress • Outlines the implications of breaches of FAIS • Describes conditions of information exchange • Stipulates the limitation of liability for losses sustained • Specifies the conditions for exemption by the Minister or Registrar

FAIS identifies four main role players which are defined in the Act as follows:

- The Financial Services Provider

"financial services provider" means any person, other than a representative, who as a regular feature of the business of such person-

(a) furnishes advice; or
(b) furnishes advice and renders any intermediary service; or
(c) renders an intermediary service

The financial services provider is any person other than a representative that either gives advice, acts as an intermediary, or both.

- The Key Individual

"key individual", in relation to an authorised financial services provider, or a representative, carrying on business as-

(a) a corporate or unincorporated body, a trust or a partnership, means any natural person responsible for managing or overseeing, either alone or together with other so responsible persons, the activities of the body, trust or partnership relating to the rendering of any financial service; or

(b) a corporate body or trust consisting of only one natural person as member, director, shareholder, or trustee, means any such natural person.

Each financial services provider will require one or more key individuals to oversee the process of providing advice and intermediary services. The key individual is any person or group of persons who are responsible for managing or overseeing the activities of the business

- The Representative

"representative" means any person who renders a financial service to a client for or on behalf of a financial services provider, in terms of conditions of employment or any other mandatory agreement, but excludes a person rendering clerical, technical, administrative, legal, accounting or other service in a subsidiary or subordinate capacity, which service-

(a) does not require judgment on the part of the letter person; or

(b) does not lead a client to any specific transaction in respect of a financial product in response to general enquiries

- The Compliance Officer

"compliance officer" means a compliance officer for an authorised financial services provider referred to in section 17 [of the Act]

Financial services providers that have one or more key individuals or representatives are required to appoint a compliance officer who must in turn provide assistance on how to comply with FAIS, report any non-compliance to the FSB, and monitor compliance.

Other key definitions within the Act are as follows:

- "advice" means, subject to subsection (3)(a), any recommendation, guidance or proposal of a financial nature, furnished, by any means or medium, to any client or groups of clients-
  - (a) in respect of the purchase of any financial product; or
  - (b) in respect of the investment in any financial product; or
  - (c) on the conclusion of any other transaction, including a loan or cession, aimed at the incurring of any liability or the acquisition of any right or benefit in respect of any financial product; or
  - (d) on the variation of any term or condition applying to a financial product, on the replacement of any such product, or on the termination of any purchase of or investment in any such product, and irrespective of whether or not such advice-
    - (i) is furnished in the course of or incidental to financial planning in connection with the affairs of the client; or
    - (ii) results in any such purchase, investment, transaction, variation, replacement or termination, as the case may be, being effected.

For the purposes of the Act "advice" does not include factual advice given: on the procedure for entering into a transaction relating to a financial product, in relation to the description of a financial product, in response to routine administration queries, in the form of objective information about a particular financial product, by the display or distribution of promotional material, or the advice given by the management board or board or trustees on the benefits of financial products.

- "financial service" means any service contemplated in paragraph (a), (b) or (c) of the definition of "financial services provider", including any category of such services

- "intermediary service" means, subject to subsection (3)(b), any act *other than* the furnishing of advice, performed by a person for on behalf of a client or product supplier-
    (a) the result of which is that a client may enter into, offers to enter into or enters into any transaction in respect of a financial product with a product supplier; or
    (b) with a view to-
        (i) buying, selling or otherwise dealing in (whether on a discretionary or non-discretionary basis), managing, administering, keeping in safe custody, maintaining or servicing a financial product purchased by a client from a product supplier or in which the client has invested;
        (ii) collecting or accounting for premiums or other moneys payable by the client to a product supplier in respect of a financial product; or
        (iii) receiving, submitting or processing the claims of a client against a product supplier.

Intermediary service does not include those services rendered by a product supplier who is authorised under a particular law to conduct business as a financial institution and where the rendering of such business is regulated by any such law, for the purposes of the Act.

- "Ombud" means-
    (a) the Ombud for Financial Services Providers appointed in terms of section 21(1); and
    (b) for the purposes of sections 27, 28, 31 and 39, includes a deputy ombud

The FAIS Act establishes the office of the Ombud for Financial Service Providers. Carter (2010) notes that the objective of the Ombud is to consider complaints in a fair, informal and economical manner and by reference to what is equitable in all circumstances. The objective of the FAIS Ombud is thus to protect consumers and ensure the integrity of the financial services industry. The FAIS Ombud will resolve any disputes that relate to the rendering of financial services by providers.

In addition to FAIS there are two codes of conduct that must be adhered to: the General Code of Conduct and the Specific Code on discretionary and administrative financial services providers. Bracher (2010) notes that fiduciary duties which were previously found only in the common law are spelt out in the General Code of Conduct. Section 2 of the General Code of Conduct provides a fundamental principle of rendering advice:

> "A provider [that is an authorized financial services provider or a representative] must at all times render financial honestly, fairly, with due skill, care and diligence, and in the interests of clients and the integrity of the financial services industry."

Noncompliance with the FAIS General Code of Conduct amounts to a breach of the FAIS Act (2002). This includes misrepresentation as provided for in Section 3 and the failure to keep record and basis of advice, as mention in Sections 8 and 9.

One of the problems with FAIS, as suggested by Bracher (2010), is that it sets the same standard for selling a simple funeral policy with a benefit of R15 000 and a major investment of R150 million making entry into the market much more difficult from the bottom up; compliance with FAIS is thus a deterrent to market entry.

2.3.2 Insurance Acts

In South Africa insurance has been regulated by two separate Acts since 1998, the Long-Term Insurance Act and the Short-Term Insurance Act. Prior to this one Act regulated both long and short-term insurance.

The short-term insurance industry as a whole is regulated by the Short-Term Insurance Act 53 of 1998 and the Long term industry by the Long-Term Insurance Act 52 of 1998. These Acts succeeded the Insurance Act of 1943, which was amended from time to time. This Act succeeded the Insurance Act 37 of 1923. Before the two Acts were passed the industry was regulated by a unified Act.

The Short-Term Insurance Act 53 of 1998 provides for the registration of short-term insurers, as well as controls the activities of short-term insurers and to much a lesser extent, intermediaries. In theory issues which deal with intermediaries should now be repealed and become regulated by FAIS.

The most significant differences between the 1998 and 1943 Acts which affect intermediaries are as follows:

- The FSB now has the power to intervene if a short-term insurance company is having financial difficulties.
- The FSB can now institute civil action against an insurance company or broker that has been accused of fraudulent or improper conduct.
- The Registrar may now impose additional policyholder protection rules, including that the contract between an insurance company and its client must be fair and there must be full disclosure.

Key definitions in the 1998 Act relating to intermediaries, which do not appear in previous acts, are as follows:

- "independent intermediary" means a person, other than a representative, who renders services as intermediary and includes a Lloyd's correspondent

- "services as intermediary" means any act performed by a person-
    (a) the result of which is that another person will or does or offers to enter into, vary or renew a short-term policy; or
    (b) with a view to
        (i) maintaining, servicing or otherwise dealing with;
        (ii) collecting or accounting for premiums payable under; or
        (iii) receiving, submitting or processing claims under, a short-term policy

- "representative" means a person employed-
    (a) by or working for a short-term insurer and receiving or entitled to receive remuneration; and
    (b) for the purpose of rendering services as intermediary in relation to short-term policies entered into or to be entered into by the short-term insurer only

It should be noted that these definitions do not coincide with the common-law definitions of employee and independent contractor.

Section 48 (which has been extensively revised) of the Short-Term Insurance Act of 1998 requires that there be a written contract between the short-term insurer and broker:

> "No consideration shall be offered or provided by a short-term insurer or a Lloyd's broker or a representative of such insurer or broker or any person on behalf of such insurer or broker or accepted by any independent intermediary, other than someone who has entered into an agreement contemplated in subsection (2), for rendering services as intermediary, and otherwise than in accordance with the regulations.

From Section 48 it should be noted that the offensive issue is only the offering and accepting of remuneration; the issue of the validity of acts committed by the broker is not an issue. The short-term insurer and/or broker who contravene this section commit an offence and is liable to a fine of R100 000.

Scrutiny of Section 48 leads to some discrepancies. A short-term insurer is defined to be a registered insurer, thus unregistered insurers do not commit offences in terms of this Section. Also, subsection (2) suggests a binding authority agreement; every broker must have binding authority failing which they cannot act as a broker. Binding authority means that the broker acts as the agent of the insurer to accept or reject without consulting with the insurer in that decision. In practice not every broker has or needs binding authority. In cases where binding authority is not granted then there is no need for the contract to be in writing.

Hopefully the revised section and the recent regulations promulgated for comment will be a vast improvement of the previous Section 48.

2.3.3 Financial services ombud schemes act

The Financial Services Ombud Schemes Act 37 of 2004 seeks to regulate the activities of the Ombudsmen. A discussion of the history and functions of ombudsmen is set out in Section 4.7. The Act provides the recognition of financial services Ombud schemes and lays down the minimum requirements of the schemes, co-ordinates the activities of the ombuds with the Pension Fund Adjudicator and the Ombud for Financial Services Providers, develops the best practices for complaint resolution, and empowers the Ombud for Financial Services Providers to act as a statutory ombud in certain cases.

Key definitions in the Act are as follows:

- "ombud" means a person who is empowered in terms of a scheme to resolve a complaint

  The task of the short-term insurance Ombudsman is to act as a mediator or arbitrator by resolving any disputes that may arise between insurers and consumers; the Ombudsman does not represent either of the parties.

- "Ombud for Financial Services Providers" means the Ombud for Financial Services Providers appointed in terms of section 21(1)(a) of the Financial Advisory and Intermediary Services Act, 2002 (Act No. 37 of 2002) and includes a deputy Ombud appointed in terms of section 21(1)(b) of that Act

- "scheme", notwithstanding any other law, means any scheme or arrangement established by or for a financial institution, or a group of financial institutions, in order to resolve a client's complaint by an Ombud-

(a) and includes any arrangement in terms of which resolution of the complaint is to be effected by mediation, conciliation, recommendation, determination or arbitration;
(b) but does not include any internal complaint resolution arrangement established by a financial institution either with or without any affiliate or subsidiary of the institution, nor the activities of the Ombud for Financial Services Providers, the Adjudicator and statutory Ombud

The role of the Ombudsman is of great importance when considering the liability of insurance intermediaries. Melville (2010) notes that although traditionally the Ombudsman's recommendations are not bindings, in South Africa the position regarding industry-based Ombudsmen (as is the case with all South African financial industry Ombudsmen) is different in that they are able to make decisions which are binding. This is discussed further in Section 4.7 of this dissertation.

2.4 *Sui generis*

The term 'sui generis' is Latin for 'of its own kind' and is used to describe something which is unique or different. In law sui generis is a legal classification that is independent to other categorizations due to its uniqueness; it is a unique set of legal rules which apply to specific circumstances.

Vivian and Liebenberg (2008) note that not all obligations can be confined to contract and delict and the instances which fall outside these two sources of obligations can be best described as *sui generis*.

3. INSURANCE OF INTERMEDIARIES

Section 2 of this dissertation explored the sources from which liability can arise and the general principles pertaining to these liabilities. This Section deals with liability as applied to insurance intermediaries and the insurance products available to mitigate these liabilities.

3.1 Insurance

Hansell (1985:5) notes that the primary function of insurance is to spread the financial losses of insured members, who unfortunately suffer a loss, over the whole of the insuring community. Insurance thus compensates the unfortunate few who have suffered a loss, at a particular point of time, from the fund contributed by the many who contribute to that fund.

A fundamental feature of insurance is risk; without risk there would be no need for insurance. Risk involves the uncertainty pertaining to whether a loss will occur and if so what the quantum of the loss will be. As most risks will have economic (financial) consequences, insurance is used as a risk-reducing mechanism in order to mitigate against the risk. Brown and Gottlieb (2001:13) note that the insurance mechanism is used to transfer the financial cost of risk from the policyholder to the pooled group of policyholders represented by the insurance corporation.

An insured is said to be 'indemnified' against loss events that are covered by the policy. The principle of *indemnity* lays down that, following a loss, an insurer should attempt to provide financial compensation *which would place the insured in the same financial position as he was in immediately before the loss* (Diacon and Carter, 1992:60). The object of indemnity is therefore to compensate the insured for a loss but not to provide the insured with a profit from the misfortune; to do so would create moral hazard problems.

Almost any risk that can be quantified can be insured against. Insurance spans across a variety of fields ranging from life insurance to general insurance. General, or non-life insurance,

includes property and liability insurance. This part of the dissertation focuses on liability insurance, specifically that of professional indemnity insurance for insurance intermediaries.

3.1 Liability insurance

Moore (1905: 319) notes that the necessity for liability insurance has for its foundation the burdens imposed upon employers by the workings of that branch of the law relating to negligence. Employer's liability insurance, an example of liability insurance, had the first policy known of its kind being issued in England in 1881. McNeely (1941) suggests the purpose of this type of insurance was not to provide compensation for injured employees but rather to protect employers against increasing litigation arising from Employers' Liability Acts.

Pantzopoulou (2003: 5) states that "liability insurance is used to provide indemnity where the policyholder is legally liable to pay compensation to a third party usually due to some form of negligence". Liability insurance is thus an insurance under which an insured insures against the risk that it will become legally liable to a third party; this liability will usually arise out of the insured's negligence.

Liability insurance differs from first party insurance in that, first party covers losses suffered by the insured person, whereas liability insurance indemnifies the insured against losses suffered by others, for which the insured is liable.[92]

Various types of liability insurance exist, the main types within the general insurance industry being:

- Employers' liability – indemnifies the employer from claims made by the employee due the employer's negligence.
- Motor vehicle third party.

[92] The distinction between first and third party liability is sometimes blurred as appeared to happen in the case of *Verulam Fuel Distributions CC v Truck & General Insurance Co Ltd* 2005 1 SA 70 W. For a discussion on the case see Vivian (2005) Cover April.

- Public liability - indemnifies the insured for legal liability arising from bodily injury or damage to property of a third party.
- Products liability – indemnifies the insured for claims for bodily harm or damage to property to a third party, due to a faulty product supplied by the insured.
- Professional indemnity – indemnifies the insured from claims made against them due to negligent professional services they provided.

This dissertation will focus specifically on professional indemnity insurance for insurance intermediaries. As the necessity for professional indemnity insurance arises due to the professionals' negligence, liability for negligence as well as professional liability will be examined.

3.1.2 Professional liability

When discussing professional liability it becomes necessary to define the meaning of a professional. Jackson and Powell (2007) note that a person will be regarded as a professional when they display four main characteristics:

- Their work is skilled and specialized
- They are committed to certain moral principles
- They usually belongs to a professional association which regulates them
- They hold a high status within the community

A professional is one who continually must exercise intellectual judgment, predicated upon high educational achievement, in the performance of his duties, and whose clients rely upon that judgment (The University of Pennsylvania Law Review; 1973: 631). For the purposes of this paper a professional is defined as an individual who performs a service for a client, the service being the professional's advice in a particular field.

Under New Jersey law, the Affidavit of Merit Statute (2002), as amended, considers licensed insurance producers to be 'professionals'.

De Villiers Hugo (1999: 130) notes that professional liability can be defined as "as individual's accountability before a court of law which may take the form either of a civil judgment for delictual [or contractual] damages to compensate for harm wrongfully caused, or of a civil judgment compelling him to refrain from continuing with an unlawful course of action, or of a criminal conviction for an offence which was found to have been committed."

The failure of a professional to perform his duties as a result of professional negligence may result in the professional being held legally liable for damages. The University of Pennsylvania Law Review (1973) notes that professional's errors are judgment is unavoidable, resulting in increasing litigation against them.

As seen in *Ultramares Corporation v Touche*[93] the long-established limit of professional liability depends on the closeness of the relationship between the professional and the client. Furthermore the extent of liability may also be established by considering those individuals who would have reasonably relied on the professional's advice.

O' Dair (1992: 405) notes that following whatever position the courts held in the 1970s and 1980s, "they are now anxious to limit the liability of the professional for his negligence to those with whom he is in a contractual relationship or one closely analogous to a contractual relationship". The University of Pennsylvania Law Review (1973: 656) also notes that the fear of economic harm due to excessive liability has often led the courts to limit narrowly liability for professional negligence.

[93] *Ultramares Corporation v Touche* 1931 255 NY 170

3.1.2.1 Duties of a professional

It has been established in law that a professional should possess a certain degree of competence as well as exercise reasonable skill and care in the performance of his or her duties. These duties, which give rise to obligations, may arise from contract, tort, statute or *sui generis*. As noted by The University of Pennsylvania Law Review (1973), the standard for professionals is that they are expected to exercise a degree of reasonable skill and care that would be attributable to other members of the same professional. In dealing with professionals, the reasonable man is a reasonable man as a professional, not the reasonable man in the street; he does not as a professional guarantee success or as far back as 1838, Tindal C.J laid down in *Lanphier v Philpos*[94] that:

> "Every person who enters into a learned profession undertakes to bring to the exercise of it a reasonable degree of care and skill. He does not undertake, if he is an attorney, that at all events you shall gain your case, nor does a surgeon undertake that he will perform a cure; nor does he undertake to use the highest possible degree of skill."

Clearly when a professional person undertakes a duty to do something, it is unlikely the defence of omissions will be of assistance. He undertakes to act positively. Over and above the positive duty to act with reasonable skill and care, the professional may be prohibited to act in certain ways by the law. Jackson and Powell (2007) note that the restrictions on the conduct of a professional fall into three categories: fiduciary obligations, undue influence, and confidentiality.

Fiduciary relationships differ from contractual and tortuous obligations in that they are based on trust. The client trusts that the professional will act in his interests. Flannigan (1989: 286) suggests that the fiduciary status is often associated with trust and 'trust-like' relationships in which conflicts of interest and duty tend to arise. The English case of *Hedley Byrne & Co. Ltd. v Heller & Partners Ltd.*[95] recognized that damages could be recovered if a fiduciary relationship existed.

[94] *Lanphier v Philpos* 1838 173 E.R. 581
[95] *Hedley Byrne & Co. Ltd. V Heller and Partners Ltd*. 1964 A.C. 465.

3.1.2.2 Contractual liability

The standard of performance of professionals has been controlled mainly by the law of contract. Usually a contract exists between the professional and his client whereby the professional agrees to perform certain services for remuneration. An implied term of this contract will be that the professional exercises reasonable skill and care. However this implied term should not be the only contractual term considered when addressing an action for professional negligence, as mentioned by Oliver J. in *Midland Bank Trust Co. Ltd. v Hett, Stubbs & Kemp*[96]:

> "The classical formulation of the claim in this sort of case as 'damages for negligence and breach of professional duty' tends to be a mesmeric phrase. It concentrates attention on the implied obligation to devote to the client's business that reasonable care and skill to be expected from a normally competent and careful practitioner as if that obligation were not only a compendious, but also an exhaustive, definition of all the duties assumed under the contract created by the retainer and its acceptance. But, of course, it is not. A contract gives rise to a complex of rights and duties of which the duty to exercise reasonable care and skill is but one."

Where a professional is retained on express terms the court may have to construe those terms to determine whether they create absolute obligations or whether the professional merely promises to exercise reasonable skill and care in undertaking a specified task or to achieve a specified result (Jackson and Powell; 2007: 12).

3.1.2.3 Tortuous (delictual) liability

As discussed in Section 3.1.1, the tort of negligence as expressed in English law, requires three conditions: a duty of care must be owed, this duty must have been breached, and damages must have been suffered as a result of this breach.

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[96] *Midland Bank Trust Co. Ltd. v Hett, Stubbs & Kemp* 1978 3 All ER 571.

A professional may owe a duty of care in tort over and above his contractual obligations. This concurrent liability has received support both for and against, however most have supported the idea, relying on Lord Macmillan in *Donoghue v Stevenson*[97]:

> "… there is the equally well-established doctrine that negligence apart from contract gives a right of action to the party injured by that negligence – and here I use the term negligence, of course, in its technical legal sense, implying a duty owed and neglected. The fact that there is a contractual relationship between the parties which may give rise to an action for breach of contract, does not exclude the co-existence of a right of action founded on negligence as between the same parties, independently of the contract, though arising out of the relationship in fact brought about by the contract."

3.1.2.4 Pure economic loss

In Section 2.2.2.5.1 it was pointed out that the courts have recognised pure economic loss as a recoverable form of damage. In this section the application of liability for pure economic loss as applied to intermediaries will be discussed.

When an intermediary is sued, the damage involved will always be pure economic in nature. As previously discussed, although delictual liability does indeed exist within modern South African case law, liability is largely subject to judicial opinion rather than objective law. The consequence of this is that the liability of intermediaries will be determined at the discretion of the courts. The case of *Jowell v Bramwell-Jones and others* 2000 (3) SA 274 SCA is a clear example of an intermediary being held liable for pure economic loss; this case will be discussed further in Section 5.2.

[97] *Donoghue v Stevenson* 1932 AC 562.

3.2 Professional indemnity insurance

Professional indemnity insurance indemnifies professionals against their legal liabilities to clients and others who rely on their advice and/or services. Hooker and Pryor (1987: 38) define professional indemnity insurance as "an insurance which indemnifies the insured professional against pecuniary loss arising out of the professional's negligent act, error or omission which causes loss to be suffered by his or her client or a third party". Indemnity cover will be provided should a client suffer a loss, whether it is material, physical or financial, which is directly attributable to the negligence of the professional.

This type of liability generally arises out of the negligent breach of contract but may also arise out of breach of statute. It hardly matters what the basis of the liability is, as long as the claim falls within the provisions of the insurance contract. The nature of the claim will differ across professions with claims commonly being for financial losses occurring as a result of advice provided. Insurers evaluate risks on individual merit and provide coverage if reasonable arguments can be made to give insurers a comfort level with the exposure (Aon; 2006: 43). Professional indemnity policies are thus designed for a specific risk and insurers will tailor a policy to the particular needs of each profession. Hooker and Pryor (1987) note that professional indemnity insurance is known by different names across different professions, such as malpractice insurance for medical professionals and Errors and Omissions (E&O) cover.

Professional indemnity insurance covers an insurance intermediary against the liability in respect of losses caused to clients by the insurance intermediary's negligence. As with any professional, the intermediary is expected to exercise a certain amount of reasonable skill and care, the failure of which will result in a breach of contract with the client entitling the client to recover compensation in the form of damages resulting from the intermediary's negligence. This duty of skill and care may also arise independently in negligence.

The Australian Law Reform Commission (1980) notes that despite the fact that the law imposes onerous duties on the intermediary in favour of the client, without professional indemnity cover a client may not be able to recover losses from an intermediary.

Professional indemnity cover for intermediaries has been made compulsory in some countries such as Australia (Queensland) and the United Kingdom.

Many variations of cover are available under professional indemnity policies; however some similarities can be found. Appendices 1, 2 and 3 provide a specimen of an international professional indemnity policy wording and a specimen of a South African professional indemnity schedule and policy wording respectively.

3.2.1 Operative clause

The operative clause describes the cover that is provided to the professional by the professional indemnity policy. The operative clause of the specimen professional indemnity policy, in Appendix 1, reads as follows:

> "The Insured named in the Schedule having applied to the Underwriters for the Insurance and having agreed that any proposal or other information supplied by the Insured or on his behalf shall be the basis of this contract of insurance, the Underwriters agree, in consideration of the payment of the premium, to bind themselves to indemnify the Insured as provided for within the Insuring Agreements of each Section of this Policy subject to the terms, Exclusions and Conditions of this Policy."

The essence of the cover is for breach of duty by reason of any negligent act or omission. The defamation cover is not negligent based and hence does not fall within the cover provided 'by reason of negligent act or omission.'

3.2.2 Claims-made cover

Prior to the 1970s, almost all liability insurance policies were written on occurrence basis. Born and Boyer (2008) note that the traditional occurrence-based insurance contract is one wherein a

policyholder is insured for liabilities from claims which occur during the period of insurance, even if the claim is not reported until after the occurrence. The coverage which is triggered with an occurrence based policy is tied to the date of the event giving rise to the claim and the policy in force when the occurrence takes place. Under this form of coverage, the policy in force on the date of the event that causes the claim responds, irrespective of when a claim is actually made. This means an insurer who writes an occurrence policy could be liable in terms of that policy, many years after the policy was issued. This insurer is thus unable to 'close' these policies.

Abraham (2001) notes that the years between 1975 and 1985 witnessed an expansion in potential civil liabilities in the United States. During this period the insurance industry suffered serious losses. The three main causes being a severe recession in the US stock markets, soaring inflation rates, and price controls which held back rate increases. Marker and Mohl (1980: 268) suggest that the combination of inflation and price controls lead to inadequate rates on current business. "In the 1970's, insurers writing professional liability insurance experienced a dramatic upswing in the late-reported claims, along with an increase in the average cost of claims that reflected the high inflation of the times, as well as other growth in costs reflecting numerous broad social trends. The industry was faced with a basic inability to accurately set the price for the occurrence policy form, because most of the claims arising out of any given year's professional services would not be reported, and thus, could not be evaluated, until well after the insurer had accepted a fixed price for an open-ended promise to indemnity" Dorroh and Whisenand (2000: 1).

Insurance prices in a competitive market vary inversely with interest rates, as a proxy for investment returns, as insurers invest the premiums they collect for long periods before the settlement of claim; Priest (1988) suggests that when interest rates drop, as they did in the mid-1980s following the decline of inflation, the cost of covering a given future payout goes up. Due to losses suffered by insurers during the 1980s and the events discussed above, most professional liability insurers switched from the occurrence policy form to the claims-made wording. The claims-made insurance wording was however adopted by the St. Paul Fire and Marine Insurance Company as well as by about one half of the physician-sponsored insurance companies during the mid-1970's, as noted by Posner (1986), however during this period occurrence coverage was

still available and was preferred by many hospitals and insurance brokers. Today, virtually all professional indemnity insurance is written on a claims-made basis.

A Claims-Made Policy indemnifies the Insured for all Claims first made (strictly speaking first reported) against them during the Policy period whether the event giving rise to the claims occurs prior to, or post, the Policy's inception date. It is assumed for this definition that retro-active cover (i.e. cover for events taking place prior to the policy's inception but resulting in claim/s during its period) has been purchased (Faure and Hartlief, 1998:699; Abraham, 1985:413). The crux of a claims-made policy is that it covers claims reported during the policy period regardless of when the event giving rise to the claim occurred. The policy trigger is therefore the date upon which the insured first reports the claim to the insurer. The policy in force at this point in time will respond to the claim, not the policy in force when the occurrence took place.

Priest (1987: 1575) notes that the claims-made provision cuts off insurance for losses resulting from the current activities of the insured that become manifest at some later period, after the insurance has expired. Furthermore a retroactive date is often specified to exclude coverage for losses that occurred prior to some specified date.

The claims-made form of coverage has been preferred to the occurrence form because, as Tuytel (2004:5) suggests, just as it is easier to determine the mother as opposed to the father of a child, it can be much less difficult to ascertain when a claim was made than when the event occurred. Thus for example in the case of an asbestos claim, the date of the claim in known, however the occurrence is difficult to determine - was it when the person worked with asbestos, or one of the years in which he worked with asbestos or when first diagnosed. Furthermore, McGuire, McCullough and Flanigan (2004) note that claims made policies were devised to manage long-tail liabilities, particularly from newly developing claims such as asbestosis claims, whereas occurrence based policies may on the other hand be exposed to long tail risks. Indeed, most professional indemnity policies are written on a claims-made form due to the long-tail exposure of many liability risks. This long-tail exposure develops when an event may go unnoticed or even unknown for a long period of time, which is the case in medical malpractice or consulting

engineers professional indemnity policies, and when the period between the occurrence giving rise to a claim and the claim being settled is relatively long and can extend to several years.

3.2.3 Limit of liability

Aickin (1986) suggests that the ability of the insurer to quantify his maximum exposure is one of the most important coverage limitations. Metcalfe (2003: 23) notes that the intent of limitation of indemnity clause is "to allocate risk in a reasonable proportion, representative of the benefits derived by the parties involved in the project". Thus this clause provides that the benefits that the professional receives are in proportion to the risk that the professional is exposed to. The clause essentially limits the insurer's exposure to the insured risk.

The limit of indemnity can be stated in the following ways, as noted by Owles and Cockerell (1986: 59):

(i) As an aggregate limit of indemnity for claims arising during any one year of insurance.
(ii) As a limit for each and every claim or series of claims arising out of the same occurrence.
(iii) The limit may be stated as both an aggregate limit and a limit for each claim.

The claim series clause states that the limit of liability will apply per claim or series of claims arising from one originating cause or source. Martignoni (2003) notes that an aggregation clause allows two or more separate losses under the policy, to be treated as one loss, if they are linked by some unifying factor.

3.2.4 Deductible

Arrow (1971) notes that coinsurance, whereby the insurer pays a stated proportion of the loss, is an effective method to reduce the risks that may arise from an insurance policy. In the professional indemnity policy, the coinsurance is affected by means of a deductible, or excess, where the insured must bear the first Rx of each and every claim.

3.2.5 Policy exclusions

Policy exclusions will narrow the scope of the insurance policy and generally exclude claims that are coverable under other forms of insurance, those risks that the insurer does not wish to cover, and restricts cover unless an extension is provided for. These exclusions can be seen in both specimen policy wordings in Appendices 1 and 3.

3.2.6 Policy extensions and conditions

The purpose of policy extensions is to broaden the scope of insurance coverage. A list of the general conditions of a South African professional indemnity policy can be seen in Appendix 3.

4. INSURANCE INTERMEDIARY

The insurance market consists of three main players: insurance providers, intermediaries, and consumers. An insurance intermediary is an individual or firm that brings together the insurance provider and the consumer. Maas (2006) notes that even with technological advances in the last few decades, the demand for intermediary services has not declined.

Cummins and Doherty (2005) note that the basic function of the intermediary is to bring together the parties of the transaction, namely the insurer and the policyholder, and match the needs of the policyholder to the products of the insurer; this is done in exchange for a commission. It should be noted that brokers are paid a commission solely for introducing insurers and insured's; insurers are in need of new business and brokers should be compensated for their role in bringing the two parties together. However, it is increasingly thought that brokers are paid commissions for their services rendered to the insured; this in theory is not the case. The very notion of a commission is for the introduction of business. If a broker is paid a fee for service, this is not a commission but a fee for service. The offering of additional services by a broker is in the

brokers own interest; it provides a competitive advantage as the insured could just as easily seek out insurance coverage himself or use the service of another broker.

Vivian (2009) notes that the fact the brokers get paid a commission for introducing business seems to have been forgotten by 'regulators', 'legislators' and judges; the case of *Afrisure CC and another v Watson NO and another*[98] 2009 2 SA 127 SCA highlights this fact. The Supreme Court of Appeal stated that brokers are paid for placing business as follows:

> "The flaw in the picture presented by De Villiers is, in my view, … [that] all the obligations listed in Annexure A would in any event be part of Afrisure's *duties as a broker*. Fundamental to De Villiers' denial that this is so was his thesis that, in principle, once a broker had successfully introduced a client to a medical scheme, he or she has no further obligations, *qua* broker, to either the client or the scheme. Departing from this premise, his proposition was that every obligation referred to in Annexure A which came after the introduction of the client to the scheme, should be classified as an additional service for which Afrisure was entitled to additional remuneration, over and above the three percent brokerage."
>
> (emphasis supplied)

From this judgment it is clear that the court thought that brokers paid for services rendered to the insured. This is a service fee (a fee for service), and not a commission in the traditional sense of the word; the court failed to understand that brokers are paid for introducing business and not for providing services. Vivian (2009) notes that as a result of this decision, brokers are deemed to not be entitled to anything for introducing business and that the entire historical role of the broker, as that of bringing the two parties together, has been obliterated. It has been forgotten.

[98] *Afrisure CC and another v Watson NO and another* 2009 2 SA 127 SCA

4.1 Economic principal-agent problem

As suggested by Eckardt (2002: 5), most insurance services are very complex experience and credence goods; specialized knowledge is required in order to correctly assess the various offers available. Therefore the need for an intermediary will typically arise due to market imperfections such as information asymmetries and transaction costs. In theory intermediaries exist because they reduce transactions costs. If it were cheaper for the two parties to locate each other and assess the products the intermediary would automatically have disappeared.

Eckardt (2002) suggests that an agency relationship exists between the insurance intermediary and the consumer; the person that engages the service of another is the principal and the insurance intermediary is the agent.[99] However because of the fact that the insurance intermediary performs functions for both the policyholder and the insurer, it could be argued that the intermediary could, for different transactions, just as easily be an agent of the insurer and indeed in many instances the intermediary could be the agent of both the insurer and the insured for different transactions. The intermediary could be the agent of the insurer to collect premiums but the agent of the insured in notifying and dealing with a claim.

As previously discussed, the principal-agent relationship will arise when the principal authorises the agent to act on his (the principal's) behalf.

A principal who does not have the expertise or skill to act on his own behalf will appoint an agent to act on his behalf. The principal-agent relationship can of course lead to the principal-agent problem, which is well known in economic theory. The principal-agent problem arises because the agent can act in his own interests to the detriment of the principal. This can occur when a 'principal' has difficulty monitoring and controlling the behaviour of his 'agent' and the agent's interests differ from those of the principal (Klein; 2000: 31), thus potentially resulting in the agent pursuing his own self-interests. The principal-agent problem, of economic theory, arises when a principal appoints an agent to act on his behalf but the agent acts on his own

[99] An agent is a person who can bind his principal in law. A broker can be an agent for specific transactions.

behalf. The principal-agent problem can manifest in terms of other well-known problems, such as the moral hazard problem. Moral hazard arises when the agent has incentives to act in his own interests and in so doing, acts against the interests of his principal who has appointed him.

The principal-agent problem, the flip side of Adam Smith's division of labour, is pervasive for which there is no clear solution. The principal-agent relationship in the economic theory sense is much broader than the principal-agent relationship in law and these two concepts should not be confused. For example in the economic sense it can be argues that the directors of a company are the agents of the shareholders. In the legal sense they are not; directors have a duty to the company and not the shareholders.

In some instances, it has been argued that a solution to the principal-agent problem would lie in compensation or remuneration structures. If the interests of the principal and the agent are aligned, so the argument goes, the principal-agent problem can be minimised. Commissions are a central feature in the incentives of intermediaries. It can be argued that commission based remuneration can promote the principal-agent problem as the intermediary may promote those insurance products that reap higher commissions where these policies are not in the interests of the insured. Thus an insured appoints an intermediary to secure the best deal but the intermediary recommends the deal which produces, for himself, the best commission. This can be done by distorting or withholding certain information.

The question is not if the principal-agent problem can exist in the insurance context. Since the problem is pervasive it can be accepted that it can and generally does exist. The question is if it is a serious problem, not in theory but in practice. Charles Rivers Associates (2001) conducted an investigation as to whether financial advisors display 'commission bias', recommending the products or providers that pay them the largest commission. The research has indicated that this problem is more prevalent to long-term insurance and especially investment products. It is less of a problem in short-term insurance where the economic agents' interests lie in a long term relationship with the insured. That this is so reinforces the incentive theory of minimizing the principal-agent problem.

When considering the principal-agent problem, it is important to realise that there is a distinction between different types of intermediaries; the impact of these differences directly affects the consequences of the principal-agent problem. The principal-agent problem is mostly found on the investment side. It is in the short-term intermediary's interest to retain a relationship with his or her client. With regard to financial and life intermediaries, however, commissions will be paid up front, therefore there is no incentive on the intermediary's behalf to maintain a long-term relationship with the client.

The principal-agent problem may also exist between the insurer (as principal) and the intermediary (as economic agent). This can arise for example where the economic agent has adverse information about an insured but in the interests of earning the commission does now disclose this to the insurer, thereby inducing the insurer to accept an insured which it would not normally accept if it knew the truth. Cummins and Doherty (2005) show that profit-based contingent commissions can help align the interests of the intermediary and the insurer thus alleviating problems that may rise from this adverse selection type of problem. Adverse selection arises because intermediaries have more information about the risks of the insured than the insurer has, but the intermediary does not disclose this information. Contingent commissions are payments made to the intermediary by the insurer based on some aggregate index of the activity placed on the intermediary, such as profitability of a book of business presented to and accepted by the insurer.

However 2004 saw the New York State Attorney General Eliot Spitzer investigating one of the world's largest brokers, Marsh & McLennan, for allegedly bid rigging in order to manipulate the market to maximize their profits. In this case, a strong argument can be made that an industry-wide ban on the contingent compensation structures targeted by Spitzer would bankrupt hundreds of small insurance agencies in communities throughout America, and lead to the further consolidation of insurance brokerage business in large global firms like Marsh (Fitzpatrick; 2006: 3042).

Legal rules and regulations will also set incentives that help overcome the conflicts of interest that may arise in the economic agency relationship. Contract law seeks to overcome problems of

asymmetry of information and stricter liability rules and regulation may provide encouragement for intermediaries to act in the interests of the insured. Eckardt (2002: 9) however notes that these rules need to be enforced in order for them to work: "if different legal rules are applied to insurance [intermediaries], different incentives are set which would result in different behaviour, eventually leading to different market outcomes".

A comprehensive treatment of the economic principal-agent problem falls outside the scope of this dissertation.

4.2 Agency law

This Section deals specifically with the application of agency law to the insurance intermediary. A problematic area in insurance law is determining on whose behalf, generally or with regard to a specific transaction, is the intermediary acting; is the intermediary an agent of the insured or the insurer? This distinction is of importance because whether or not the intermediary is the agent of the insurer or the insured affects the insured's right of recourse should the contract fail; under general agency principles, the intermediary's actions are imputed to the principal.

Richmond (2004) notes that how an intermediary is classified will affect an insurance companies' potential liability in disputes arising from the intermediaries actions because insurers are only liable for the tortious actions of their agents within the course and scope of their agency; thus if the intermediary is acting as the agent of the insured, negligence cannot be imputed on the insurer. Havenga (2001) further notes that distinguishing whether the insurance intermediaries is acting on behalf of the insured or the insurer is useful as it recognizes that the law of agency is of primary concern when defining the legal position of insurance intermediaries.

If the intermediary is acting on the insured's behalf then the intermediary's behaviour is deemed to be one and the same as the insured's. Thus if the intermediary is at fault, if for example, the intermediary makes a misrepresentation on the proposal form, then the insurer can avoid the policy on the grounds of breach of contract regardless of the insured's actions.

If the intermediary acts on behalf of the insurer then, for example, whatever information is conveyed to the intermediary, the insurer is deemed to have the same knowledge; whether or not the insurer is actually aware of the information is irrelevant. Thus the insurer becomes liable for the actions of the intermediary. It is important to note that in this instance, when dealing with the insurance intermediary, the insured is, in essence, dealing with the insurer; no distinction is made between the two.

To over simplify, [an insurer] may be able to avoid liability if it is determined that the intermediary was not the agent of the insurer, and it was the actions of the intermediary that caused the dispute (Ziomek and McCahill; 1999: 69).

As discussed in Section 2.1.3, the agency relationship is one where the agent has express or implied consent to act on behalf of the principal when arranging contracts with third parties. The principal gives the agent consent, or 'authority', to act on his behalf. Authority will take one of three forms: actual (express or implied) authority, apparent authority, or authority arising from ratification.

Due to the complex role of the intermediary in the insurance transaction, the intermediary can effectively 'change sides' depending on the transaction. The same person can thus represent both the insured and the insurer but it is doubted if that can be done legally satisfactorily involving the same transaction. Lloyd's brokers have attempted to be the agent for both parties when it comes to dealing with claims and the courts have expressed dissatisfaction about this, nut the matter remains unsolved. This is commonly referred to as 'transferred agency'.

Rao and Rajah (2000) suggest the following criteria are often used in determining whether the intermediary is the agent of the insured or the insurer:

- who first requests the intermediary's services;
- who controls the intermediary's actions;
- whose interest is being protected by the intermediary; and

- who pays the intermediary (however in most instances the intermediary will be paid by the insurer unless a fee has been otherwise negotiated).

From case law, however, it has been established, generally, that the insurance intermediary is the agent of the insured and not the insurer when placing the insurance business; *Rozanes v Brown*[100] and *Roberts v Plaisted*[101]. In *Searle v A.R. Hales*[102] it is further noted that despite any close relationship between the intermediary and the insurer, the intermediary will remain the agent of the insured.

However, there exist certain circumstances where the intermediary acts as the agent of the insurer. Three examples of exceptions to the general rule when the intermediary will be regarded as an agent of the insurer are as follows:

1) The intermediary has been given actual authority by the insurer, for example to collect the premium.
2) The intermediary may have authority to bind the insurer to cover, as in *Stockton v Mason.*[103] This is where the intermediary is given so-called binding authority.
3) The intermediary is the appointed representative of the insurer.

An insurance intermediary on South Africa is increasingly required to sign a contract with the insurer and thus is bound by the laws of agency to the insurer, who is essentially the principal with regard to the specific transactions mentioned in the agreement. The purchaser of insurance will also expect the intermediary to act with his best interests in mind. The insurer will expect the intermediary to put its interests before those of the insured for those transactions where the intermediary is the agent of the insurer. Duska (2005) notes that the question of whose agent the intermediary is, is a legal wrangle rather than an ethical one. Whose agent the intermediary is, is usually a question of fact to be determined by the actual circumstances of the case. Sometimes as in South Africa with the now repealed S20bis legislation could be of assistance in determining

[100] *Rozanes v Brown* 1928 32 Lloyds Law Rep 98 (CA).
[101] *Roberts v Plaisted* 1989 2 Lloyd's Law Rep 341.
[102] *Searle v A.R. Hales* 1995 CLC 738.
[103] *Stockton v Mason* 1978 2 Lloyd's Rep 430.

the issue. Om the cases involving the winding-up of the AA Mutual the legislation was decisive. The court concluded that the intermediary was the agent of the insuer for the collection of insurance premiums. Thus in that case all premiums collected and held by the intermediary belonged to the insurer. If the intermediary is to act in the best interest of the insurer, then the best interests of the insurer should as far as possible coincide with the best interests on the insured, thus the intermediary should in essence, in most instances, act in the best interests of both parties. The role of legislation will become of increasing importance once the currently discussed binder regulations come into force.

4.2.1 United States

Insurance law is a State matter, the preserve of each state in the United States; however the acts of an intermediary are governed by the principles of the law of agency which are fairly consistent throughout the various states.

The case of *Hardin, Rodriguez & Boivin Anesthesiologists Ltd. v Paradigm Insurance Co.*[104] sets out the criteria for determining who an intermediary is acting on behalf of:

1) Who first set the intermediary in motion
2) Who controlled the intermediary's actions
3) Who paid the intermediary
4) Whose interest was the intermediary to protect

State courts have held that an agent acts for the insurer in the formation stages of a contract. In *Saunders v Allstate Insurance Co*.[105] the Supreme Court of Ohio found that where an intermediary provided the insurer with false information the insurer could be estopped and thus avoid liability.

[104] *Hardin, Rodriguez & Boivin Anesthesiologists Ltd v Paradigm Insurance Co.* 1992 962 F.2d 628.
[105] *Saunders v Allstate Insurance Co*. 1958 151 NE 2d 1.

In the United States it is generally accepted that an intermediary acts on behalf of the insurer when collecting policy information implying that the insured will not be held liable for any faults of the intermediary in these circumstances.

California:

Under the agency agreement the agent is deemed to act for the insurer as stipulated in Section 731 and 1704 of the California Insurance Code. However, as seen in *Maloney v. Rhode Island Ins.*[106], the insurance broker acts for the insured and not the insurer.

Delaware:

The Delaware Title 18 Insurance Code distinguishes between agents and brokers and provides the following: under Section 1702 an agent who solicits or negotiates insurance shall be deemed the agent of the insurer and under Section 1703 a broker who acts or aids in negotiating insurance shall be deemed to be representing the insured.

Georgia:

The courts determined in *Kirby v. Northwestern Nat'l*[107] that a broker is an independent agent and as such represents the insured and not the insurer. Furthermore, it was held in *European Bakers Ltd. v. Holman*[108] that if the insured relies on an independent insurance agent when choosing an insurer then the independent agent is the agent of the insured. However an agent may act for both the insured and the insurer through dual agency if both parties consent.

[106] *Maloney v. Rhode Island Ins.* 1953 115 Cal. App. 2d 238, 244, 251 P.2d 1027
[107] *Kirby v. Northwestern Nat'l* 1994 213 Ga. App. 673, 445 S.E.2d 791
[108] *European Bakers Ltd. v. Holman* 2004 177 Ga. App. 172, 338 S.E.2d 702

Idaho:

As a general rule the agent of the insurer is not the agent of the insured, subject to statutory and contractual provisions; *Sysco International Food Serv. V. City of Twins Falls*[109].

Indiana:

As seen in *Benante v. United Pacific Life Ins. Co.*[110] the insurer is generally not liable for the acts of an agent who is a broker and the determination of whose agent the intermediary is depends on the facts of the situation.

Iowa:

The Iowa Code Section 515.105 provides that within the agency relationship "any officer, insurance producer, or representative" of an insurance company is deemed to be the agent of the insurer.

Kansas:

The insurance agent is the agent of the insurer and not the insured, and as such the insurer is liable for any misrepresentation relating to the coverage available on a policy sold; *Stewart v. Commonwealth Cas. Co.*[111]

Massachusetts:

As seen in *Hudson v. MPIUA*[112] the insurance agent represents the insurance company and the insurance broker is the agent of the insured. However, according to the Massachusetts General

[109] *Sysco International Food Serv. V. City of Twins Falls* 1985 109 Idaho 88, 91, 705 P.2d 548, 551
[110] *Benante v. United Pacific Life Ins. Co.* 1995 659 N.E.2d 545, 547.
[111] *Stewart v. Commonwealth Cas. Co.* 1933 137 Kan. 919, 22 P.2d 435.
[112] *Hudson v. MPIUA* 1982 386 Mass. 450, 436 N.E.2d 155.

Laws Chapter 175 Section 169, an insurance agent or broker who negotiates or renews a policy of insurance will hold the premium as the agent of the insurer.

Montana:

The insurance broker is generally regarded as the agent of the insured; *Nautilus Ins. v. First Nat'l Ins. Inc.*[113]

Nebraska:

Fadden v. Sun Ins. Co.[114] held that an agent may act for both the insurer and the insured so long as the agent's duties do not conflict.

New Jersey:

The insurance broker acts as the agent of the insured; *Rider v. Lynch*[115].

New York:

As a general rule the broker is the agent of the insured, however the determination of whether the agent acts for the insured or the insurer is a question of fact; *Jet Setting Service Corp. v. Toomey*[116].

Ohio:

The Ohio Insurance Code Section 3911.22 provides that a solicitor of insurance will be considered the agent of the company and not the insured should any controversy between the insured and the company arise.

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[113] *Nautilus Ins. v. First Nat'l Ins. Inc.* 1992 254 Mont. 296, 837 P.2d 409.
[114] *Fadden v. Sun Ins. Co.* 1933 124 Neb. 712, 248 N.W. 62.
[115] *Rider v. Lynch* 1964 42 N.J. 465, 201 A.2d 561.
[116] *Jet Setting Service Corp. v. Toomey* 1983 91 A.D.2d 431, 459 N.Y.S.2d 751

Oklahoma:

The Oklahoma Code provides in Title 36 Section 1435.3 that every insurance producer shall be regarded as the agent of the insurer and not the insured in any controversy between the insured and the insurer.

South Dakota:

The South Dakota Code stipulates in Title 58 Section 30-175 that “no insurance producer or business entity may act as an agent of an insurer unless the insurance producer becomes an appointed insurance producer of that insurer”.

Wyoming:

According to Wyoming Statutes Section 26-1-102, the insurance agent acts on behalf of the insurer and the insurance broker acts on behalf of the insured.

4.2.2 Australia

The law of Australia follows the common law agency principles as those in the United Kingdom. The Australian Law Reform Commission published a Report on agents and brokers in 1980, implemented by the Insurance (Agents and Brokers) Act 1984, which briefly mentioned the principles of agency.

The Insurance (Agents and Brokers) Act contains the following definitions:

> “insurance broker” means a person who carries on the business of arranging contracts of insurance, whether in Australia or elsewhere, as agent for intending insured’s

> "insurance intermediary" means a person who-
>
> a) for reward; and
>
> b) as an agent for one or more insurers or as an agent for intending insured's,
>
> arranges contracts of insurance in Australia or elsewhere, and includes an insurance broker

No definition is given for an 'insurance agent' though the term 'insurance intermediary' is taken as including both broker and agent. The Insurance (Agents and Brokers) Act was however repealed in 2004 when the Financial Services Reform Act 2001 was enforced, the above definitions however remained.

The Insurance (Agents and Brokers) Act states that generally the insured must bear the responsibility of the broker. The insurer's responsibility is limited to the conduct of the intermediary which is within the actual or apparent authority of the agent. Furthermore there may be some circumstances where the insurer may be held liable for the conduct of the intermediary notwithstanding the fact that for the most part the intermediary is the agent of the insured in the law of agency.

The case of *Norwich Union Fire Insurance Society Ltd. v Brennans*[117] highlights those factors which the courts take into consideration when deciding agency issues. In this case Mr. Justice Lush offered the following guide concerning the difference between a broker who acts for the insured and an insurance agent who acts for the insurer:

> "Neither of these is a term of precision but the broad distinction is between a person, firm or company which carries on an independent business of placing insurance upon the instructions of clients whose basic relationship of agency is with the client, and the insurer's agent whose function is to procure persons to insure with his principal, the insurer, and whose basic relationship of agency of therefore with the insurer"

[117] *Norwich Union Fire Insurance Society Ltd. v Brennans* 1981 VR 981.

The Australian Law Reform Commission suggests two main areas where the issue of the insurer's responsibility for the conduct of the intermediary arises: first at the time of arranging the policy and second on the completion of the proposal form.

4.2.3 New Zealand

The Law Reform Act 1977 sets out when an insurance intermediary is deemed to be acting on behalf of the insurer and when the insurer will be responsible for the actions of the intermediary. It states that when the insurance intermediary acts for the insurer during the negotiation of a contract, within the scope of his actual or apparent authority, then the intermediary will be the agent of the insurer.

Certain flaws in this Act have however been identified:

a) The agency status is determined by whether the intermediary receives remuneration or not.
b) The agency status only applies to the insurer's deemed knowledge of the information disclosed to the intermediary by the insured.
c) The intermediary is not required to disclose to the insured whether he is an agent of the insurer or not.

4.2.4 Hong Kong

No professional standards for insurance intermediaries are imposed in Hong Kong, and there are no restrictions in a person setting up a business an insurance intermediary. The Law Reform Commission of Hong Kong (1986) suggests that although the intermediary is generally the agent of the insured, the intermediary may also be the agent of the insurer at all material times. The Commission further suggests that a code of conduct be established where the intermediary is required to inform the insured in what capacity he is acting.

4.2.5 Israel

Articles 32 to 36 of the Insurance Contract Law (1981) address the status of the insurance broker. An 'insurance agent' is defined as:

> "anyone who carries out the business of insurance broking between Assureds and Insurers."

The Insurance Contract Law (1981) further provides the position of the insurance broker:

a) When negotiating the conclusion of an insurance contract, the insurance broker will be the agent of the insurer unless acting upon an insured's written request.
b) The insurance brokers' knowledge of material facts will be regarded as the insurer's knowledge.
c) For the purposes of the receipt of insurance premium, the insurance brokers will be regarded as the agent of the insurer.
d) The insurance broker will be regarded as the agent of the insurer for the purposes of notice by the insured or the beneficiary to the insurer.

The Insurance Business Control Law (1981) (or the Control Law) provides that an insurance broker is an intermediary between the insurer and the insured but does not distinguish between different types of brokers within the insurance market. The Control Law further specifies the situations where the insurance broker provides the services of an agent, are governed by agency law; these are extremely similar to those laid out in the Insurance Contract Law (1981). The insurance broker is regarded as the insurer's agent unless the insured has given a written request for the broker to act as his representative for the purposes of negotiation only. Thus when considering duty of disclosure, the insurance brokers' knowledge concerning any material information is also regarded as the insurers knowledge.

The status of the Israeli broker thus differs from the status of most European brokers in that in most European cases the broker is usually deemed to be the agent of the insured even though he receives a commission from the insurer.

However, in *Aryeh Insurance Co. of Israel Ltd. v Kaplansky*[118] the Supreme Court rejected the allegation that, in terms of the Insurance Contract Law (1981), the insurance broker is considered to be the agent of the insurer and thus the insurer should be held liable for the broker's wrongdoings. The court held that the law does not provide a general assumption that the broker is the insurer's agent but rather suggests that this relationship occurs in three specific circumstances: during negotiations, for purposes of disclosure, and in the receipt of payments.

4.2.6 Canada

The Insurance Act (2000) of Alberta provides in Section 503 that an insurance agent is deemed to be the agent of the insurer under the contract for the purposes of receiving any premium for a contract of insurance.

4.3 Role and duties

The insurance intermediary in bringing the two parties together, more often than not also acts as a professional insurance adviser. The intermediary should possess sound knowledge of insurance practices and the insurance industry and provide its clients advice on such. The intermediary will undertake to perform certain tasks and be given certain responsibilities on behalf of its principal. The precise nature of the intermediary's duties will depend on the terms of his appointment.

Lechner and Raturi (2004: 3) note that the role of the insurance intermediary has evolved from merely matching the buyer of insurance to the seller to include both services for clients and insurance companies and furthermore that these services "go beyond the structuring and placement of insurance cover". The intermediary will typically assess the risk of a client, structure the insurance program, negotiate with the insurer, and handle the policy administration, claims management and risk management services. Mintzer (2009) suggests that a 'special relationship' exists between the client and the insurance intermediary which will create a

[118] *Aryeh Insurance Co. of Israel Ltd. v Kaplansky* LCA 2281/05.

heightened duty on the insurance producer to advise their clients and Medoway (2002) further emphasizes the paramount importance of the fiduciary relationship between the insurance intermediary and the client.

The insurance intermediary will have certain obligations to the insured; Shub and Hopley (2007) note that these include, amongst others:

- Taking reasonable steps to obtain the cover desired by the insured
- Obtaining all relevant information about the risk of the insured
- Exercising skill and care in selecting a reputable insurer
- Giving advice on policy exceptions and obligations
- Giving legal advice

Moreover the intermediary will also have obligations to the insurer and third parties.

Christensen (1990: 39) notes that whereas the insurance *agent* owes a primary duty as the agent of the insurer to the insurer (under general agency laws), the insurance *broker* owes a primary duty to the insurer, however even though there exists statutory differences between insurance agents and brokers, when determining the intermediary's liability, these distinctions are generally ignored by the courts. However, Christensen (1989) suggests that removal of this distinction will result in unexpected liability being imposed upon the insurance intermediary.

4.3.1 Standard of care

An insurance intermediary's basic duty of care will arise out of the contract of agency between the insured and the intermediary where the intermediary must exercise reasonable skill and care in the performance of his functions. Arnould, Mustill and Gilman (1981) state that "[i]n no case does the law require an extraordinary degree of skill on the part of the agent, but only such a reasonable and ordinary degree as persons of average capacity in his situation and profession might fairly be expected to exert. In enquiries, therefore, as to his liability in case of loss, the

question is, whether the act or omission complained of is inconsistent with that reasonable and proper degree of care, skill and judgment which persons of common prudence or ordinary ability might be expected to show in the situation and profession of the defendant".

The New Jersey Supreme Court in *Wang v. The Allstate Ins. Co. et al*[119], citing *Rider v. Lynch*[120] stated that:

> "One who holds himself out to the public as an insurance broker is required to have a degree of skill and knowledge requisite to the calling. When engaged by a member of the public to obtain insurance, the law holds him to the exercise of good faith and reasonable skill, care and diligence in the execution of the commission. He is expected to possess reasonable knowledge of the types of policies, their different terms, and the coverage available in the area in which his principal seeks to be protected. If he neglects to procure the insurance, or if the policy is void or materially deficient or does not provide the coverage he undertook to supply, because of his failure to exercise the requisite skill or diligence, he becomes liable to his principal for the loss sustained thereby."

Shub and Hopley (2007) suggest that the current trend in the insurance industry appears to be that insurance intermediaries are increasingly being discharged of their obligations in the duty of care.

The question arises: does the intermediary's duty of care extend to third parties? That is, will the law impose a duty of care on the intermediary where a third party has suffered a financial loss as a result of the intermediary's act?

The case of *BP plc v Aon Limited & Aon Risk Services of Texas Inc.*[121] dealt with the issue of whether and to what extent a sub-broker owes a duty of care to the insured when there is no contractual relationship between the two parties. Here the court found that such a duty of care does exist in tort.

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[119] *Wang v. The Allstate Ins. Co.* 1991 et al 125 N.J. 2, 592 A.2d 527.
[120] *Rider v. Lynch* 1964 42 N.J. 465, 476, 201 A.2d 561, 567.
[121] *BP plc v Aon Limited & Aon Risk Services of Texas Inc.* 2006 EWHC 424 (Comm).

Christensen (1990) suggests that there are potentially four levels of care imposed upon insurance intermediaries:

1) Generalist – all intermediaries must exercise reasonable skill and care whether the agent of the insured or the insurer.
2) Specialist or expert – the intermediary possess more credentials and expertise.
3) Professional – a degree of care must be exercised as expected from others of the same profession, held to a higher standard of performance.

The emergence of 'expert' status as the standard by which to measure the conduct and performance of an insurance agent is far removed from an early determination that an insurance agent is engaged in a mere business or occupation rather than being engaged in a profession (Ziomek and McCahill; 1999: 66).

In *Darner Motor Sales v. Universal Underwriters*[122] the Arizona Supreme Court held that insurance intermediaries must exercise a professional standard of care:

> "The principle involved here is simply that a person who holds himself out to the public as possessing special knowledge, skill or expertise must perform his activities according to the standard of his profession… Insurance agents cannot be considered as professional without assuming the responsibilities and duties generally associated with such a status. One of those responsibilities is to exercise that degree of care ordinarily to be expected from others in their profession."

4.3.2 Duty of disclosure

It is a matter of basic law that the intending insured must disclose to the insurer every material matter relating to the risk being insured against (Westgarth; 1984: 37). One of the tasks of the

[122] *Darner Motor Sales v. Universal Underwriters* 1984 140 Ariz. 383, 682 P.2d 388.

insurance intermediary may be to assist the insured, who may not understand this duty, to discharge the duty to disclose material information when effecting insurance; this is illustrated by Reynolds JA in *Fanhaven Pty. Ltd. v Bain Dawes Northern Pty. Ltd:*[123]

> "The obligation of disclosure in respect of contracts of insurance is not widely known or understood by laymen. The ordinary person who answers the question in a proposal form honestly and to the best of his ability believes that no more is required of him. Even if there is reference to material facts or to matters likely to affect the risk this is virtually meaningless to the ordinary person. This being the position, the signing of the proposal involves a concealed trap. The duty of disclosure is a persuasive duty and a failure involves drastic consequences. One of the reasons a broker is employed is so that a valid and enforceable contract is procured and if the broker does not alert his client to the pitfalls he fails to exercise due care and skill because whilst he knows of the requirements of the law in this respect the unwary client does not and the agent therefore fails to use his best endeavours to procure that which he was employed to procure."

Under common law the parties are required to disclose all material facts; an insured must disclose all facts which a prudent insurer would consider to be material when deciding whether to grant insurance. An insurer may avoid a contract under common law for breach of duty of disclosure. As in the case of negligence, the agent will be liable for the amount of loss unless the insurer would have issued a policy even if it knew the information (Ziomek and McCahill; 1999: 69).

4.3.3 Fiduciary duties

Intermediaries will, in general, owe a duty of a fiduciary; as such they owe a duty of skill and care as implied in their contract as well as a duty to act *bona fide* in a manner they deem to be in the best interest of their customers. Quinn (2001: 23) notes that insurance intermediaries will have fiduciary duties to policyholders, prospective policyholders or insurers and further explains

[123] *Fanhaven Pty. Ltd. v Bain Dawes Northern Pty. Ltd.* 1982 2 NSWLR 57.

the nature of fiduciary duties: "A owes B a fiduciary duty when A has the highest possible duty of loyalty and good faith. A as a fiduciary of B, must place the interests of B ahead of its own. A breaches its fiduciary duties to B whenever he places his own interests ahead of B… Someone can breach fiduciary duties negligently".

Birds and Hird (2001: 186) note that the fiduciary relationship carries with it strict duties, in particular the overriding one that the fiduciary, the agent, must not put himself into a position where his own interests do or may conflict with his duties to his principal. Furthermore, under the rules of agency law, as a fiduciary duty is owed to the principal, the agent is in a special position of trust which imposes a duty of loyalty upon the agent (Christensen; 1990).

In England, matters concerning fiduciary duties are regulated by the Financial Services Authority (FSA) (1998) and are known as the 'Principles of Business' or 'Core Principles'. These principles state that firms, including insurance intermediaries, must conduct business "with integrity" and organize its affairs "with due skill, care and diligence". Furthermore the firm must "pay due regard to the interests of its customers and treat them fairly"; this includes managing conflicts of interests fairly.

Moreover a person in a fiduciary position is not entitled to make a profit or put himself in a position where his interests and his duties conflict. The FSA (2008) states in the Insurance Conduct of Business Sourcebook (ICOBS) in Section 4.4.3 that "… the essence of these fiduciary obligations is generally a duty to account to the agent's principal. But where a customer employs an insurance intermediary by way of business and does not remunerate him, and where it is usual for the firm to be remunerated by way of commission paid by the insurer out of premium payable by the customer, then there is no duty to account but if the customer asks what the firm's remuneration is, it must tell him".

4.4 Vicarious liability and the liability of the principal for the acts of the agent

Laski (1916: 106), a very early writer on the subject, notes that the age has passed when each man might bear untroubled the burden of his own life; to-day, the complexities of social

organization seem, too often, to cast us, like some Old Man of the Sea, upon the shoulders of our fellows. Vicarious liability is a tort doctrine and a form of strict liability; it will arise when one person is held liable for the damage done by another person to a third person.

The American Law Institute (1958) provides the following definitions in Section 2 of the Restatement of Agency:

1) A master is a principal who employs an agent to perform service in his affairs and who controls or has the right to control the physical conduct of the other in the performance of the service.
2) A servant is an agent employed by a master to perform service in his affairs whose physical conduct in the performance of the service is controlled or is subject to the right to control by the master.
3) An independent contractor is a person who contracts with another to do something for him but who is not controlled by the other nor subject to the other's right to control with respect to his physical conduct in the performance of the undertaking. He may or may not be an agent.

It is further mentioned that the term 'independent contractor' encompasses those persons who contract to do something for another but are not servants in doing the work; thus an agent who is not a servant is an independent contractor and moreover, a broker who contracts to sell a product for a principal is an independent contractor. Although, under some circumstances, the principal is bound by the broker's unauthorized contracts and representations, the principal is not liable to third persons for the tangible harm resulting from his unauthorized physical conduct within the scope of the employment., as the principal would be for similar conduct by a servant; nor does the principal have the duties or immunities of a master towards the broker (The American Law Institute; 1958: §2).

Atiyah (1967) notes that it is only in the master-servant relationship that vicarious liability, proper, will be imposed in all situations, that is to say, strictly in the employer-employee relationship rather than the general principal-agent relationship. Sykes (1984) notes that the

principal will not be vicariously liable for the torts committed by a non-servant or an independent contractor unless the principal was negligent, the tortfeasor acted under the principal's apparent authority, or the tort arose from a dangerous activity.

Problems arise when distinguishing whether to apply the law of agency or vicarious liability to determine if the principal is liable for the acts of the agent as the two are very similar. McCarthy (2004: 9) notes that the law is unclear as to the interplay between agency concepts and vicarious liability. Both involve situations in which the act of one person (*A*) may create obligations on the part of a second person (*P*) toward a third person (*T*) (Reese and Flesch; 1960: 764) where, in agency, *A*'s act may result in obligations from *T* to *P* and *P* to *T* but in vicarious liability the act may make *P* liable to *T* however *P* will not have any rights against T. Thus a three-way relationship is created between *A* and *T*, *T* and *P*, and *A* and *P*.

If vicarious liability is to be applied to the principal-agent relationship (where the insurance company is a 'principal' and the independent agent is an 'agent'), this would essentially mean that insurers could be held liable for the acts of the agents with whom they do business as noted by Sandler, Klubes and Barloon (1999), a form of liability known as *respondeat superior*.

The Queensland Law Reform Commission (2001: 4) notes that it is not always clear whether the liability of a principal for an agent's tort is vicarious or personal (that is, a breach of one's own duty), however liability will usually be personal:

- where the wrongful act was specifically instigated, authorised or ratified by the principal;
- where the wrongful act amounts to a breach by the principal of a personal duty, liability for non-performance or non-observance of which cannot be avoided by delegation to another.

Martignoni and Hopley (2008) note that the High Court of Australia has rejected numerous cases that attempted to expand the liability of a company for the negligence of an independent contractor. The courts have accepted the authority in *Colonial Mutual Life Assurance Society*

Ltd. v Producers and Citizens Co-operative Assurance Company of Australia Ltd.[124] that a company will only be held vicariously liable for the torts committed by a contractor if the contractor is an agent of the company. In the *Colonial Mutual Lif*e case the High Court [of Australia] held an insurance company vicariously liable for damages resulting from defamatory statements made by its representative about another insurance company while acting in his representative capacity (Pilner; 1978: 484).

However, in *Sweeney v Boylan Nominees Pty. Ltd.*[125] the High Court of Australia found the independent contractor not vicariously liable for his negligence as he was not an employee. "In *Sweeney* the majority gave an extremely narrow operation to *Colonial Mutual Life,* holding that the decision stands only for the proposition that a principal will be held liable for slanders made by an independent contractor 'engaged to solicit the bringing about of legal relations between the principal and third parties', and even then only when those slanders are made in order to persuade the third party to enter legal relations with the principal. This interpretation of *Colonial Mutual Life* is based on the concept of agency: the insurance salesman was the principal's agent ('properly called so') and the tortuous conduct occurred during the execution of that agency" (Burnett; 2007: 168). Kirby J however found in minority that the principal was liable on the grounds of agency. The majority stated that:

> "… the wider proposition [in *Colonial Mutual Life*] that underpinned the argument of the appellant in this case, that if A 'represents' B, B is vicariously liable for the conduct of A, is a proposition of such generality that it goes well beyond the bounds set by notions of control or set by notions of course of employment."

In contrast with Australian case law involving the same insurance company in the same year, South African case law does not recognize vicarious liability for torts of persons other than employees, as seen in *Colonial Mutual Life Assurance Society Ltd. v Macdonald*[126]. The Court held unanimously that the insurance company was not liable for damages arising out of the

[124] *Colonial Mutual Life Assurance Society Ltd. v Producers and Citizens Co-operative Assurance Company of Australia Ltd.* 1931 46 CLR 41.
[125] *Sweeney v Boylan Nominees Pty. Ltd.* 2006 HCA 19.
[126] *Colonial Mutual Life Assurance Society Ltd. v Macdonald* 1931 AD 412.

negligent driving of its representative while taking a medical practitioner to examine a proponent for a life insurance policy (Pilner; 1978: 484), as the insurance agent was seen to be acting as an independent contractor and not as a servant at the time on question.

McKendrick (1990) suggests that agents may be viewed as a new type of independent contractor and that an employer will be liable for torts committed within the scope of authority. The difference between an employee and an independent contractor is often described as that between a contract *of* service, made between employer and employee, and a contract *for* services, made between principal and independent contractor (Burnett; 2007: 166). However the difficulty arises in drawing a clear distinction between the agent and the employee, and also between the agent and the independent contractor.

Sandler, Klubes and Barloon (1999) suggest that as an employer is generally not liable for the acts of an independent contractor; in order for an insurer to avoid liability it must be proven that the agent is in fact an independent contractor and not an employee.

In determining whether the principles of vicarious liability apply to the principle-agent relationship the definition of an agent becomes important as the broader the scope of the term, the greater the scope of potential vicarious liability. Gleeson CJ notes in *Scott v Davis*[127] that:

> "… to describe a person as the agent of another, in this context, is to express a conclusion that vicarious liability exists, rather than to state a reason for such a conclusion. Nevertheless, some judges refer to agency as a criterion of liability, similar to employment. If that is to be done, it is necessary to be more particular as to what is meant."

Dal Pont (2001) recognizes three categories of agency:

- those that create legal relations between principals and third parties;
- those that affect legal relations between principals and third parties; and
- those that have authority to act on behalf of the principal.

[127] *Scott v Davis* 2000 204 CLR.

An insurance agent in the sense of a representative of the company empowered to negotiate contracts of insurance on its behalf may be employed by an insurance company as an employee on a contract of service, and the fact that he is employed to establish contractual and commercial relations between his principal and members of the public does not preclude him from being a servant (Pilner, 1978: 483).

McCarthy (2004) suggests that vicarious liability is generally accepted to exist in cases where an agent represents a principal in transactions with a third party. Lindgren J relied on *Colonial Mutual Life Assurance Society Ltd. v Producers and Citizens Co-operative Assurance Company of Australia Ltd.*[128] when stating in *NMFM Property Pty. Ltd. v Citibank Ltd.*[129] that:

> "In Australia, the general principle is established that where [a principal] appoints [an agent] as [the principal's] agent to persuade persons to a contract with [the principal], [the principal] will incur liability to [a third party] if [the agent] makes tortuous statements that are within the general class or scope of statements that [the principal] authorised [the agent] to make, and put [the agent] in a position to make."

The State of California in the Unites States has held in *Gibson v. Government Employees*[130] that as the broker is the agent of the insured, the insurer cannot be held vicariously liable for the broker's negligence.

There is much disagreement in agency law as to when a principal will be liable for the acts of his agents. A fundamental element of confusion that arises is whether a principal (who is not a master) is *generally liable* for the torts of his or her agent (who is not a servant), on the basis of vicarious liability *or* otherwise (McCarthy; 2004: 10).

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[128] *Colonial Mutual Life Assurance Society Ltd. v Producers and Citizens Co-operative Assurance Company of Australia Ltd.* 1931 46 CLR 41.
[129] *NMFM Property Pty. Ltd. v Citibank Ltd.* 2000 186 ALR.
[130] *Gibson v. Government Employees* 1984 162 Cal. App. 3d 441, 208 Cal Rptr. 511

4.5 Damages

Jackson and Powell (2007) suggest that the breach of a duty by an insurance intermediary will either take the form of: a breach of a contractual duty, a breach of an implied contractual duty, a breach of a duty of care owed, or a breach of a statute.

The general remedy for the breach of a duty by the insurance intermediary is an award for damages whereby the insured should be placed in the same position he would have occupied had the non-payment by the insurer not occurred. "In contract this means that the insured should be compensated as if the contract had been properly performed; in tort it is as if the tortuous act occasioning the loss had not taken place, so that a valid contract of insurance existed. This principle can, however, only be applied where the broker's error was sufficiently proximate to cause the loss, and that the loss that occurred was sufficiently foreseeable" (Henley; 2004: 410).

Henley (2004) and Jackson and Powell (2007) both emphasize the importance of the 'causation' element in brokers' liability as the brokers defences will usually consist of one of three forms (generally containing some form of contributory negligence by the insured):

(i) That the insured would not have been insured regardless of any failure of the broker.
(ii) That the insured would not have obtained the required insurance had all the facts been known.
(iii) That the insured somehow contributed to the lack of suitable insurance.

Kerr J. made a distinction between total avoidance due to the insured's breach and voidability where the insurer could choose to treat the policy as void in *Everett v Hogg, Robinson and Gardner Mountain (Insurance) Ltd.*[131]. Henley (2004: 415) notes that in cases of avoidance *ab initio* the insured had to prove that he would have been paid, effectively on an *ex gratia* basis since no obligation to pay could exist, whilst in cases of voidability the broker had to prove that the insurer would have elected to avoid the policy and refuse to pay all or part of the claim to the insured.

[131] *Everett v Hogg, Robinson and Gardner Mountain (Insurance) Ltd. 1973 2 Lloyd's Rep. 188*

The Law Reform (Contributory Negligence) Act 1945 of the United Kingdom provides an apportionment of liability in cases of contributory negligence which states the following:

> "Where any person suffers damage as the result partly of his own fault and partly of the fault of any other person or persons, a claim in respect of that damage shall not be defeated by reason of the fault of the person suffering the damage, but the damages recoverable in respect thereof shall be reduced to such extent as the court thinks just and equitable having regard to the claimant's share in the responsibility for the damage"

Thus allowing that damages which are recoverable by the insured due the brokers' negligence to be reduced to what is considered just and equitable by the court, taking into consideration the insured's responsibility in causing the damage.

Furthermore, Jackson and Powell (2007: 1204) state that if the client enters a reasonable compromise of his claim against the insurers, the measure of loss against the broker is the difference between what he actually recovered from insurers and what he would have recovered had the broker not been negligent.

4.6 Regulation

Bester, Chamberlain, Short and Smith (2006) note that insurance is regulated in order to protect consumers and correct information asymmetries and will be imposed in the market in one of three ways: by regulating who may enter the market (institutional regulation), what products may be sold (product control regulation), and how the products must be sold (functional regulation). Mayerson (1965: 51) suggests that insurance is regulated for two purposes: solvency and equity, with solvency being the main aim "because of the intangible nature of the insurance contract and the fact that, until a claim actually occurs, all the policyholder has to show for his hard-earned premium is a piece of paper - a promise to pay which he relies on and believes will be honoured in the event that he ever has need for the coverage promised by his insurance policy".

Due to the fact that a consumer may have imperfect information, the State may decide to intervene by imposing regulations in order to help the consumer make economically rational decisions. As previously mentioned, in the purchasing of insurance there exists an asymmetry of information between the insured, the insurer, and the intermediary. The complexity of the insurance product as well as the fact that it is a credence good magnifies the asymmetry of information. Hence the policyholder needs protection against unscrupulous or inadequately financed insurers, against excessive premium rates, against small print in the policy, and against misleading advertising or sales presentations which might induce him to buy a policy he doesn't need or, worse, to buy the wrong policy (Mayerson; 1965: 51). Thus the State may impose regulations in order to protect consumers.

The Australian Law Reform Commission (1980) suggests that the problems faced by the insured when seeking to recover from the intermediary for any losses suffered may be reduced under appropriate regulatory rules which stipulate financial procedures and professional indemnity requirements.

4.6.1 Australia

Queensland has regulated intermediaries since 1916 with the Insurance Act 1916. This Act contains the following definitions:

> "Agent" – A person licensed to act as the agent of one or more insurers in the transaction of marine or general insurance business
> "Broker" – A person licensed to act as the agent of the insured in the transaction of marine or general insurance business with the Commissioner, or any insurer

In New South Wales the law relating to disclosure and misrepresentation is stipulated in Section 18 of the Insurance (Amendment) Act 1983:

> 18A Misrepresentation and non-disclosure

A contract of insurance that is entered into, reinstated or renewed after the commencement of this section is not void, voidable or otherwise rendered unenforceable:

a) by reason only of a false or misleading statement made in or in connection with the contract or a proposal, offer or document that led to the entering into, reinstating or renewing of the contract unless the statement was material to the insurer in relation to the contract of insurance and-
   (i) the statement was fraudulent; or
   (ii) the insured knew or a reasonable man in his circumstances ought to have known that the statement was material to the insurer in relation to the contract of insurance; or
b) by reason only of an omission of matter from the contract or a proposal, offer or document that lead to the entering into, reinstating or renewing of the contract unless the matter omitted was material to the insurer in relation to the contract of insurance and-
   (i) the omission was deliberate; or
   (ii) the insured knew or a reasonable man in his circumstances ought to have known that matter material to the insurer in relation to the contract of insurance had been omitted.

The New South Wales Law Reform Commission (1983) suggests that Section 18 is designed to allow the insured to receive indemnity despite the contrary terms of the contract; it allows for the failure to perform a condition of the contract to be excused by the court should the insured not be prejudiced in any way. Westgarth (1984: 39) notes that the most significant feature of this section is the alteration of the common law test for materiality whereby the false statement or omission must be material to the *actual* insurer rather than a *prudent* insurer and further suggests that "for the broker, the section has the effect that he may be unaware of the particular idiosyncrasies or peculiar requirements of the actual underwriter with whom he is dealing".

The Australian Law Reform Commission (1980) suggests that the main argument in favour of the regulatory control over intermediaries is related to competence and fitness of the intermediary.

The principal legislation governing the interpretation of insurance contracts in Australia, however is the Insurance Contracts Act 1984. Section 54 of this act provides that an insurer may not refuse to pay claims in certain circumstance and reads as follows:

1) Subject to this section, where the effect of a contract of insurance would, but for this section, be that the insurer may refuse to pay a claim, either in whole or in part, by reason of some act of the insured or of some other person, being an act that occurred after the contract was entered into but not being an act in respect of which subsection (2) applies, the insurer may not refuse to pay the claim by reason only of that act but the insurer's liability in respect of the claim is reduced by the amount that fairly represents the extent to which the insurer's interests were prejudiced as a result of that act.
2) Subject to the succeeding provisions of this section, where the act could reasonably be regarded as being capable of causing or contributing to a loss in respect of which insurance cover is provided by the contract, the insurer may refuse to pay the claim.
3) Where the insured proves that no part of the loss that gave rise to the claim was caused by the act, the insurer may not refuse to pay the claim by reason only of the act.
4) Where the insured proves that some part of the loss that gave rise to the claim was not caused by the act, the insurer may not refuse to pay the claim, so far as it concerns that part of the loss, by reason only of the act.
5) Where:

    (a) the act was necessary to protect the safety of a person or to preserve property; or
    (b) it was not reasonably possible for the insured or other person not to do the act;

    the insurer may not refuse to pay the claim by reason only of the act.

6) A reference in this section to an act includes a reference to:

    (a) an omission; and

(b) an act or omission that has the effect of altering the state or condition of the subject-matter of the contract or of allowing the state or condition of that subject-matter to alter.

Pesce (2003) notes that the insurance industry has argued that Section 54 of the Insurance Contracts Act 1984 should be reformed as it threatens the availability of insurance and increase premiums, and further mentions that in the case of *FAI General Insurance Company Limited v Australian Hospital Care Pty. Ltd.*[132] the High Court held that FAI was liable for a claim even though the policy stipulated that the insured had to notify them of the claim as Section 54 applied.

Merkin (2006: 61-62) notes that Section 54 "is wide-ranging, extending to any contractual obligation which has 'the effect' of entitling insurers to refuse to pay a claim, including provisions governing the assured's conduct during the currency of the policy (encompassing risk definition insofar as it is based on an act or omission of the assured, continuing warranties and other obligations such as reasonable care clauses) and provisions which regulate the assured's conduct in the claims process… The result is to treat all policy obligations or restrictions affecting the assured's conduct, whether in the form of risk definition, continuing warranties, conditions or otherwise, in exactly the same way, because they all have the same effect of entitling the insurers to refuse to pay a claim". It should be noted that this Section overrides the Claim Circumstances Reporting clause and thus converts the policy, in respect or circumstances, to a losses occurring basis.

4.6.2 United States

In the United States regulation is governed at state level. Christensen (1990: 38) notes that due to the McCarran-Ferguson Act, there is no federal regulation of the insurance industry; however the states regulate who may sell insurance and what policies may be sold.

[132] *FAI General Insurance Company Limited v Australian Hospital Care Pty. Ltd.* 2001 HCA 38

The Federal McCarran-Ferguson Act (1945) provides in Section 1012 (a) and (b) respectively that the "business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business" and that "no Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance". It essentially upholds the Federal principle that the states can regulate insurance without federal interference.

The Act was passed in response to the Supreme Court case of *United States v. South-Eastern Underwriters Association*[133] where the court held that an insurance company that conducted business across state lines, thus engaging in interstate commerce, was subject to federal antitrust regulation. The McCarran-Ferguson Act was enacted due to the states' concerns that they no longer had the authority to regulate insurance. The positions in some of the states are now examined.

4.6.2.1 Arizona

Statutory definitions of the Insurance Producer Licensing Act 2001 were extensively revised with the Arizona Revised Statutes in 2002. Under Section 20-281 an 'insurance producer' is now inclusive of both agents and brokers and is defined as a person licensed to sell, solicit or negotiate insurance. The terms for which an Insurance Producer may be eligible for a license are provided as well as the terms of the denial, suspension or revocation of an Insurance Producers license.

4.6.2.2 Georgia

The Official Code of Georgia Annotated (OCGA) provides in Section 33-23-41 that if an agent procures insurance contracts for an insurer who is not authorized to do business in the State then the agent "shall be held personally liable to the same extent as the insurer upon every contract of insurance made by the insurer with reference to a risk having a situs in [the Georgian] state, if

[133] *United States v. South-Eastern Underwriters Association* 1944 322 U.S. 533.

the [agent] participated in the solicitation, negotiation, or making of the contract or in any endorsement to the contract, in any modification of the contract, or in the collection or forwarding of any premium or portion of the premium relating to such contract."

4.6.2.3 Kentucky

The Kentucky Code defines an agent in Chapter 304.9-020 as "an individual or business entity appointed by an insurer to sell or to solicit applications for insurance or annuity contracts or to negotiate insurance or annuity contracts on its behalf", however no statutory definition is provided for a broker of insurance.

The Kentucky Code further provides in Chapter 304.9-035 that the insurer is liable for the acts of its agent when "the agents are acting in their capacity as representatives of the insurer and are acting within the scope of their authority.

4.6.2.4 New Jersey

The N.J.S.A, commonly known as the Affidavit of Merit Statute, was enacted in 1995 in order to reduce the filing of frivolous negligence claims and ensures that only certain cases that meet a threshold proceed in the litigation process. This statute was amended in 2002 to include 'insurance producers' classified as "any person who solicits, negotiates or sells contracts of insurance".

4.6.3 Canada

Similar to that of the United States, in Canada insurance regulation is provided by each individual province.

Ontario:

The Registered Insurance Brokers of Ontario (RIBO) was established in 1981 as a self-regulatory body for insurance brokers in Ontario to protect the public when entering into insurance transactions with intermediaries. RIBO regulates the professional and ethical conduct, licensing, and financial obligations of all independent insurance brokers in the province of Ontario.

In Ontario insurance intermediaries are regulated by the Registered Insurance Brokers Act. This Act provides a Code of Conduct in Section 14 of Ontario Regulation 991 for intermediary's that stipulates the standard of professional conduct for registered insurance brokers:

> 14. All members shall act as insurance brokers in accordance with the following code of conduct:

1. A member shall discharge the member's duties to clients, members of the public, fellow members and insurers with integrity.
2. A member owes a duty to the member's client to be competent to perform the services which the member undertakes on the client's behalf.
3. A member shall serve the member's client in a conscientious, diligent and efficient manner and shall provide a quality of service at least equal to that which members would generally expect of a member in a like situation.
4. A member shall be both candid and honest when advising the member's client.
5. A member shall hold in strict confidence all information acquired in the course of the professional relationship concerning the business and affairs of the member's client, and the member shall not divulge any such information unless authorized by the client to do so, required by law to do so or required to do so in conducting negotiations with underwriters or insurers on behalf of the client.
6. A member shall observe all relevant rules and laws regarding the preservation and safekeeping of property of the client entrusted to the member and, when there are no such rules or laws or the member is in doubt, the member must take the same care of such

property as a careful and prudent person would take of the person's own property of like description.

7. A member who engages in another business or occupation concurrently with the practice of the member's vocation shall not allow such outside interest to jeopardize the member's integrity, independence or competence.

   7.1 A member shall disclose in writing to a client or prospective client any conflict of interest or potential conflict of interest of the member that is associated with a transaction or recommendation.

8. A member shall not stipulate, charge or accept any fee that is not fully disclosed, or the basis for which is not fully disclosed prior to the service being rendered, or which is so disproportionate to the service provided as to be unconscionable.
9. A member shall encourage public respect for and try to improve the practice of the member's vocation.
10. A member shall make the member's services available to the public in an efficient and convenient manner which will command respect and confidence and which is compatible with the integrity, independence and effectiveness of the member's vocation.
11. A member shall assist in maintaining the integrity of the member's vocation and should participate in its activities.
12. A member shall assist in preventing the unauthorized practice of the member's vocation.
13. A member's conduct towards other members, members of the public, insurers and the Corporation shall be characterized by courtesy and good faith. R.R.O. 1990, Reg. 991, s. 14; O. Reg. 410/04, s. 4.

Furthermore Section 15 of Ontario Regulation 991 provides the following definition of 'misconduct' which will warrant disciplinary action by the Disciplinary Committee of RIBO:

15. (1) For the purposes of the Act,

"misconduct" means any of the following:

1. The use of methods of solicitation and advertising that are not compatible with the honour and dignity of the vocation including, without limiting the generality of the foregoing, the use of any illustration, circular or memorandum that misrepresents, or by omission is so incomplete that it misrepresents the terms, benefits or advantages of any policy or contract of insurance issued or to be issued, and the making of any false or misleading statement as to the terms, benefits or advantages of any contract or policy of insurance issued or to be issued.
2. The use of any incomplete comparison of any policy or contract of insurance with that of any other insurer for the purpose of inducing, or intending to induce, an insured to lapse, forfeit or surrender a policy or contract.
3. The use of any payment, allowance or gift, or any offer to pay, allow or give, directly or indirectly, any money or thing of value as an inducement to any prospective insured to insure.
4. Directly or indirectly making or attempting to make an agreement as to the premium to be paid for a policy other than as set forth in the policy, or paying, allowing or giving, or offering or agreeing to pay, allow or give, a rebate of the whole or part of the premium stipulated by the policy or any other consideration or thing of value intended to be in the nature of a rebate of premium to any person insured or applying for insurance in respect of person or property in Ontario, but nothing in this paragraph shall be construed to affect any payment in the nature of a dividend, bonus, profit or savings that is provided for in the policy.
5. Coercing or proposing, directly or indirectly, to coerce a prospective buyer of insurance through the influence of a professional or business relationship or otherwise to give a preference that would not otherwise be given on the effecting of an insurance contract or coercing, inducing or exercising undue influence in order to control, direct or secure insurance business.
6. Holding oneself out or advertising by means of advertisements, cards, circulars, letterheads, signs, or other methods, or carrying on business in any other manner than the name in which the individual or the corporation or partnership of which the individual is the designated representative is registered.

7. The use of any practice or conduct that results in unreasonable delay or resistance to the fair adjustment of claims.
8. Failure to carry on business in a manner consistent with the code of conduct.
9. Failure to comply with the provisions of the Act and this Regulation.
10. Acting as an insurance agent or holding himself, herself or itself out, advertising or conducting himself, herself or itself in such a manner as to lead a reasonable person to believe that the member is an insurance agent.
11. Being convicted, after the 1st day of October, 1981, of a criminal offence or an offence under the *Insurance Act*, whether or not the offence was committed before the 1st day of October, 1981.
12. The payment of any referral fee or finder's fee to, or the acceptance of a referral fee or finder's fee from, a person who is not,

    (i) licensed as an insurance agent or broker under the laws of any jurisdiction,
    (ii) licensed to sell mutual funds under the laws of any jurisdiction,
    (iii) licensed as a real estate agent or broker under the laws of any jurisdiction,
    (iv) licensed as a mortgage broker under the laws of any jurisdiction,
    (v) engaged in the business of a financial planner,
    (vi) engaged in the business of providing financing for the payment of insurance premiums, or
    (vii) engaged in the business of providing products or services that reduce insurance risk.

13. A registered insurance broker who is a director, officer or principal broker of a corporation that is a member or who is a partner or principal broker of a partnership that is a member or who is the principal broker of a sole proprietorship that is a member has knowingly concurred in the misconduct of the sole proprietorship, partnership or corporation.
14. Providing false or misleading information to the Corporation.
15. Acting as a principal broker as described in section 7.2 when the member has failed to comply with the educational requirements established by the Council under that section.

16. Failure as a principal broker to properly supervise brokers whose registration is restricted to acting under his or her direction and supervision. R.R.O. 1990, Reg. 991, s. 15 (1); O. Reg. 72/96, s. 4; O. Reg. 410/04, s. 5.

    (2) Nothing in this section shall be construed to prohibit a member from being licensed as and acting as a life insurance agent under the *Insurance Act*. R.R.O. 1990, Reg. 991, s. 15 (2).

Alberta:

Alberta is governed by the Insurance Act (2000) which provides in Section 1(bb) that an insurance agent is one who, for compensation:

i. Solicits insurance on behalf of an insurer, insured or potential insured,
ii. Transmits an application for insurance from an insured or potential insured to an insurer,
iii. Transmits a policy of insurance from an insurer to an insured,
iv. Negotiates or offers to negotiate on behalf of an insurer, insured or potential insured or the continuance or renewal of insurance on behalf of an insurer or insured, or
v. Enrolls individuals in prescribed contracts of group insurance but does not include an insurer

Further the Act stipulates in Section 488 that an insurance agent will be considered a broker only if the agent is party to two or more subsisting agency contracts with different insurers and none of these agency contracts requires that the agent deal with only one insurer.

Alberta is further regulated by the Insurance Act: Insurance Agents and Adjusters Regulation (2001) which provides the necessary classes and levels of certificates of authority for insurance agents.

New Brunswick:

Section 369 (2) of the Insurance Act R.S.N.B. (1973) provides that an agent or broker is personally liable to the insured on all contracts of insurance unlawfully made by or through him directly or indirectly with any insurer not licensed to undertake insurance in the Province, in the same manner as if the agent or broker were the insurer.

Newfoundland:

Section 25 (1) of the Insurance Adjusters, Agents and Brokers Act (1990) provides that an agent, broker or representative is liable to the insured on all contracts of insurance unlawfully made through the agent, broker or representative directly or indirectly with an insurer not licensed to undertake insurance in the province in the same manner as if the agent, broker or representative were the insurer.

Nova Scotia:

Insurance agents are governed by Part III of the Insurance Act R.S.N.S. (1989) which provides that an agent or broker is personally liable to the insured on all contracts made by or through him directly or indirectly with any insurer not licensed pursuant to Section 6 to carry on the business of insurance in the Province in the same manner as if the agent or broker were the insurer.

Quebec:

An Act Representing Market Intermediaries (1998) which essentially provided the concept of insurance agents and insurance brokers being ‘market intermediaries’ was replaced with An Act Representing the Distribution of Financial Products and Services R.S.Q. Chapter D-9.2. (DFPSA) which provides the concept of an ‘insurance representative’ instead. An insurance representative is defined in Section 2 as either “a representative in insurance of persons, a group insurance representative, a damage insurance agent or a damage insurance broker”. The distinction between agent and broker is thus made only with regard to damage insurance,

providing definitions of each in Section 5 and 6 respectively. Section 130 further provides that an insurance representative who does not act for a firm and is not an employee of an independent partnership may act as an independent representative.

The Autorité des marches financiers (AMF) is the body mandated by the Quebec government to regulate financial markets as well as assist consumers. The DFPSA provides in Section 200 that the AMF may regulate the terms of the issuance of representatives certificates.

4.6.4 New Zealand

The Insurance Intermediaries Act 1994 provides the following definitions:

> Broker, in relation to an insurer, means a person-
>
> a) Who carries on the business of arranging contracts of insurance (whether or not the business is the person's principal business or is carried on in connection with any other business; and
> b) Who is not the employee of the insurer; and
> c) Who is not appointed, under a signed agreement, as the agent for the insurer for the purposes of receiving money due to the insurer from the insured and due to the insured from the insurer
>
> Insurance intermediary –
>
> a) Means a person-
> (i) Who for reward arranges contracts of insurance in New Zealand or elsewhere; and
> (ii) Who does so as the employee of or agent for one or more insurer or as the agent for the insured; and
> b) Includes a broker.

This Act provides for, *inter alia*, the payments to insurance intermediaries, the duties of brokers in relation to premiums, and the duties of brokers in relation to payments due to the insured.

The Insurance Law Reform Act of 1977 provides the following in Section 10:

> 10 **Salesman, etc, to be agents of insurer**
>
> 1) A representative of the insurer who acts for the insurer during negotiation of any contract of insurance, and so acts within the scope of his actual or apparent authority, shall be deemed, as between the insured and the insurer and at all times during the negotiations until the contract comes into being, to be the agent of the insurer.
> 2) An insurer shall be deemed to have notice of all matters material to a contract known to a representative of the insurer concerned in the negotiation of the contract before the proposal of the insured is accepted by the insurer.
> 3) In this section the term **representative of the insurer** includes any servant or employee of the insurer and any person entitled to receive from the insurer commission or other valuable consideration in consideration for such person's arranging, negotiating, soliciting, or procuring the contract of insurance between a person other than himself and such insurer.

This Section intends to make the insurance intermediary who acts for the insurer during the negotiations of the insurance contract the agent of the insurer and, in so doing, puts the liability of a non-disclosure by the insured to the intermediary on the insurer.

4.6.5 United Kingdom

Up until the 1950's captive (tied) agents distributed insurance products in the United Kingdom; captive (tied) agents work exclusively for one insurance company. Independent brokers only emerged in this market after the 1950's, when they did not charge for advice giving, and gained most of the market share in the 1980's and 1990's; they are today the largest distribution channel of insurance products. The regulation of intermediaries only emerged in 1977 with the Insurance Brokers (Registration) Act.

The Financial Services and Markets Act 2000 (FSMA) is an Act of Parliament that created the Financial Services Authority (FSA); the FSA regulates all financial services providers including insurance providers.

In the United Kingdom the intermediary's conduct is regulated by both statute and codes of conduct. The FSMA defines an insurance intermediary as follows:

> "a person who, in the course of any business or profession, invites other persons to make offers or proposals or to take other steps with a view to entering into contracts of insurance with an insurer other than a person who only publishes such invitations on behalf of or on the order of some other person"

The regulation seeks to provide consumers with greater knowledge however it also increases costs for insurers.

4.6.6 European Union

The Insurance Mediation Directive (IMD) was adopted on 9 December 2002 and was introduced as a set of requirements for the regulation of European Union (EU) insurance intermediaries. The IMD permits EU insurance intermediaries to operate in other member states on a freedom of service basis thus aiding the functioning of a single market for insurance. The IMD provides the following definitions:

> 'insurance mediation' means the activities of introducing, proposing or carrying out other work preparatory to the conclusion of contracts of insurance, or of concluding such contracts, or of assisting in the administration and performance of such contracts, in particular in the event of a claim.
>
> 'insurance intermediary' means any natural or legal person who, for remuneration, takes up or pursues insurance mediation;

Abril, Gonzalez and Aguirre (2007) note that the new law is based on three fundamental ideas:

i. the regulation of insurance intermediaries (classified as insurance agents, insurance brokers, and bank insurance operators)
ii. the creation of a homogenous regime to carry out insurance intermediation activities
iii. the protection of consumer rights in private insurance intermediation services.

All 27 member states (including France, Germany, Portugal and Spain) have implemented the IMD.

4.6.7 South Africa

Regulation of the South African insurance intermediaries', according to Bester et al (2006) involves controlling the type and quality of the company offering insurance and intermediation as well as controlling the methods that must be used in effecting the insurance. The insurance intermediaries' market in South Africa is regulated by an ever increasing array of legislation including the Short-Term Insurance Act, the Long-Term Insurance Act, the Medical Schemes Act, the Pension Funds Act and especially the Financial Advisors and Intermediary Services Act; these Acts have been discussed in Section 2.4 of this dissertation. In addition to these Acts regulations are promulgated in terms of the Acts. The regulation on the insurance market in South Africa seeks to inform and protect consumers.

The Short-Term Insurance Act also seeks to control the price of intermediary services; according to the Act intermediaries cannot charge prices that exceed a certain threshold amount. Commissions are accordingly regulated, which has been a source of difficulties.

Prior to the late 1990's the intermediaries' market was not heavily regulated with regard to intermediaries being able to enter the market without any formal registration. FAIS was introduced in 2002 in order to regulate advice-giving and the intermediary's servicest. FAIS has effectively enhanced the quality of the intermediary service, however Bester *et al* (2006) suggest that it has also raised the cost of giving advice in the following ways:

- Increased barriers to entry by the exclusion of certain potential entrants who fail to meet qualifying criteria means that the cost of entering the market increases.
- Increased infrastructure costs due to the fact that the intermediary must now comply with minimum infrastructure requirements increases costs directly.
- Compliance and reporting costs increases the cost of business of the intermediary.
- Increased transaction costs increases the cost of business for the intermediary.

Section 16(1) of FAIS provides that a Code of Conduct that must be drafted and adhered to by all financial services providers and their representatives to:

a) act honestly and fairly, and with due skill, care and diligence, in the interests of clients and the integrity of the financial services industry;
b) have and employ effectively the resources, procedures and appropriate technological systems for the proper performance of professional activities;
c) seek from clients appropriate and available information regarding their financial situations, financial product experience and objectives in connection with the financial service required;
d) act with circumspection and treat clients fairly in a situation of conflicting interests; and
e) comply with all applicable statutory and common law requirements applicable to the conduct of business.

Furthermore Section 16(2) provides that the Code of Conduct must also contain provisions relating to adequate disclosures of material information, appropriate record-keeping, avoidance of fraudulent and misleading advertising, safe-keeping of funds, and professional indemnity cover.

4.7 Ombudsman

As previously discussed in Section 2.5.3, the purpose of the insurance ombudsman is to resolve the disputes that arise to policyholders whose claims have been rejected, as regulated by the Financial Services Ombud Scheme Act in South Africa. The task of the Ombudsman is to act as a 'mediator' or informal arbitrator between the parties of a dispute. This Section deals with general aspects pertaining to the Ombudsman, and more importantly the liability imposed on insurance intermediaries arising from the Ombudsman's rulings.

4.7.1 South Africa

In South Africa the first insurance Ombudsman established was in 1985 for long-term insurance. Following this, the Office of the Ombudsman for Short-Term Insurance was established in August 1989. These were voluntary ombudsmen. The Office of the Pension Funds Adjudicator was established in January 1998 in order to investigate and decide on complaints in terms of the Pension Funds Act. Unlike the two insurance ombudsmen, the Pension Funds Adjudicator is a statutory institution.

In 1999 a Council was established that confirmed the independence of the Ombudsman Office, the main function being to facilitate the timely and fair dispute resolution process. Section 20 of the FAIS Act (2002) which states that when dealing with complaints the Ombud is "independent and must be impartial". It is the FAIS ombudsman that deals with insurance intermediaries.

Section 27 of the FAIS Act (2002) deals specifically with the receipt of complaints, prescription, jurisdiction and investigation with regard to the Ombud for financial service providers and provides in sub-section 5 that:

The Ombud –

a) may, in investigating or determining an officially received complaint, follow and implement any procedure (including mediation) which the Ombud deems appropriate, and allow any party the right of legal representation;

b) must, in the first instance, explore any reasonable prospect of resolving a complaint by conciliated settlement acceptable to all parties;
c) may, in order to resolve a complaint speedily by conciliation, make a recommendation to the parties, requiring them to confirm whether or not they accept the recommendation and, where the recommendation is not accepted by a party, requiring that party to give reasons for not accepting it: Provided that where the parties accept the recommendation, such recommendation has the effect of a final determination by the Ombud, contemplated in section 28(1);
d) may, in a manner that the Ombud deems appropriate, delineate the functions of investigation and determination between various functionaries of the Office; -
e) may, on terms specified by the Ombud, mandate any person or tribunal to perform any of the functions referred to in paragraph (d).

Section 28(1) provides that where a matter has not been settled then the Ombud must make the final determination which may include the dismissal or upholding of the complaint, either wholly or partially, and furthermore states that the Ombud "may make any other order which a court may make".

The Financial Services Ombud Schemes Act (2004) provides that the FAIS Ombud may act as a statutory Ombud and as such may determine which scheme ombudsmen may deal with a complaint, should a dispute over the jurisdiction of the ombudsmen arise. Furthermore, a FAIS Ombud, acting as a statutory Ombud, may investigate and adjudicate a complaint that a scheme ombudsmen has no jurisdiction over. Furthermore Section 13(2) provides the following:

> (a) No Ombud of a recognised scheme has jurisdiction to resolve a complaint or settle a matter in respect of which the Adjudicator or the Ombud for Financial Services Providers has jurisdiction in terms of a law, except in the case of any such complaint in respect of which the Adjudicator of the Ombud for Financial Services Providers has in terms of a law declined to resolve the complaint or settle the matter.

It is important to note that the Ombudsman's Office is an independent office and all the Ombudsman's decisions are binding on the insurance company but not the insured. Furthermore the Ombudsman's rulings are based on law and proper insurance practice (i.e. fair dealing and equity). The decisions can be based on either law or on equity and as such the determinations are completely at the discretion of the Ombudsman.

It should be further noted that the standing of the Ombudsman in terms of the judicial system is below that of the Magistrates Court and that rulings of the Magistrates Courts are not published, however the Ombudsman usually makes determinations that are widely publicized. This will undoubtedly expose the rulings of the Ombudsman to attack on review or appeal (Melville; 2010).

The success of the Office lies in the acceptance, by the industry, of the Ombudsman's rulings. Bester *et al* (2006) suggest that the rulings of the FAIS Ombud are focused on consumer protection. Melville (2010: 56) suggests that although the Ombudsman, is in some quarters, expected to have a consumer advocacy role, neutrality is paramount.

Since the inception the various ombudsmen and adjudicators have made a large number of determinations, most of which can be found on the various websites. For the purpose of this dissertation it is unnessecary to discuss these in detail. There is a growing perception that these determinations are becoming increasingly pro-consumer, anti-business and not strictly in terms of the law. The argument has always been that the determinations are guided more by equity than law. The concept of the Ombudsman is still fairly young internationally and little understood in South Africa (Melville; 2010: 65). Time will tell if these perceptions are correct and if the swing is too far in favour of consumers. It should be noted that the pro-consumer bias differs from scheme to scheme. Some of these rulings are now discussed.

4.7.1.1 *VA Mes v Art Medical Equipment Pension Fund*

The case of *VA Mes v Art Medical Equipment Pension Fund*[134] involving a Pension Funds determination was widely discussed. A pension fund 'trustee' was for the first time held liable in his personal capacity to a member. Vivian (2006) notes that the Pension Fund Adjudicator (PFA) system operates in a different manner to our traditional legal system in that the PFA system is like a trial by correspondence where the law is put forward by the PFA himself.

The complainant's late husband, Peter Mes, was employed by a company that went into liquidation after his death. Peter Mes was both employed by Art Medical Equipment (Pty.) Ltd. and was a member of the Art Medical Equipment Pension Fund. The sole trustee of the fund was M G Thobois, the managing director of the company, and his son Francis Thobois was the general manager. In terms of the fund's rules, all benefits under the fund were secured by a policy of assurance concluded with Liberty Life. Upon the death of Peter Mes, a death benefit became payable. The family of Peter Mes contacted Liberty Life in December 1998 to inform them of his death, however Liberty advised that the premiums were in arrears and thus they would not pay the claim.

In August 2001 a rule *nisi* was issued by the PFA for the fund and Liberty Life to show cause why they should not be held to pay the risk benefits. The PFA ruled that "the conduct of the employer and the trustee in this matter has been grossly negligent, if not dishonest". Furthermore, if Liberty could show that they were not liable for the death benefits then "the trustee of the fund, M G Thobois will be personally liable". Moreover the general manager of the fund could also be held personally liable for other reasons. Both the trustee and the general manager were never party to the dispute but were being held liable by the Adjudicator, as noted by Vivian (2006). To quote from another well known case, the Adjudicator 'showed a red card to a spectator'. The position held in 2001 was that no order was made against the trustee or employer but Liberty Life was ordered to furnish the trustee and general manager with copies of the preliminary determination.

[134] *VA Mes v Art Medical Equipment Pension Fund* Case No: PFA/GA/1198

However in 2005 the issue resurfaced with the trustee and the general manager as co-respondents. Vivian (2006) notes that since no order was ever made against them, it would have seemed that the claim against them had prescribed many years ago and furthermore that since the premiums had not been paid, the policy had lapsed before Peter Mes had died; Liberty was not liable under this view which is the view of the traditional legal system.

A rule *nisi* was made in 2005 that the trustee was indeed liable to pay the risk benefits and should the trustee holds that he is not liable then he should explain why within a short period of this new ruling being handed down. The ex-trustee did reply however he was found to be liable by the PFA in the final determination in 2006.

In his reply the trustee asserted that the procedure in dealing with the claim was both unfair and untenable, and that the time frame in which to reply was too short. The PFA however rejected these statements. Vivian (2006) highlights the issue that sufficient funds were indeed available in the employers reserve to pay the outstanding premium, and due to the case not being argued in the traditional manner, the significance of this point is lost. Furthermore if Liberty Life had paid the outstanding funds, as it had been advised by its broker to do, then the policy would not have lapsed. The PFA however decided that he had no jurisdiction over intermediaries, and because of the lack of jurisdiction, the trustee should be liable. Vivian (2006) suggests that the PFA system as it stands is unsatisfactory and that the system should be rethought, possibly with a review to the High Court.

4.7.1.2 *Maduray v Action Plan Management and Renasa Insurance Company*

The determination of the FAIS ombud in *Maduray v Action Plan Management and Renasa Insurance Company*[135] against an intermediary and also an insurer has left the jurisdiction of the FAIS ombud as uncertain.

[135] *Maduray v Action Plan Management and Renasa Insurance Company* Case number: FOC4250/06-07/KZN (3)

The complainant's motor vehicle was comprehensively insured by Renasa through Action Plan Management (APM), the intermediary. An accident occurred in 2006 whilst the insured was driving, damaging the vehicle beyond economical repair. A claim was thus lodged by the insured. Renasa repudiated this claim on the basis that the tracking device in the vehicle recorded a speed of 161km/h at the time of the accident which was above the legal speed limit; the insured had thus been in breach of a specific warranty in the policy, the good Citizen Warranty which states that a claim for damages will be waived if the vehicle is used contrary to the laws of South Africa.

The complainant referred the matter to the Short-Term Ombudsman who determined that the insurer could not be faulted and also suggested that the FAIS Ombud , who had jurisdiction over intermediaries, could be approached. This lead to the determination by the FAIS Ombud in 2008, in favour of the complainant, against both the intermediary and the insurer. Vivian (2009) suggests that as a point of insurance law, it is difficult to fault the conclusion originally arrived at by the Short-Term Ombud that Renasa validly repudiated the claim.

The complainant held that she was unaware of the warranty and had not been informed of this warranty by the broker; however the broker held the insured had been advised on this matter. The FAIS Ombud concluded that the insured had not been advised. Vivian (2009) notes that it is difficult to pin point the basis of the Ombud's findings as the determination is "wide, ranging and divergent".

Furthermore, the Ombud held the insurer jointly and severely liable with the broker; the basis of this liability, as stated by Vivian (2009), is unclear. The FAIS Ombud held that the insurer had the same responsibilities as the intermediary and as such became liable in the same way as the intermediary stating that:

> "Neither of the respondents made [the] complainant aware of the warranty…"

As mentioned by Vivian (2009: 62), insurers are insurers, and not intermediaries; the consequences for an insurer who does not draw attention to clauses in a policy are different than those of the intermediary:

> "If an intermediary does not inform the insured of a term in the policy, the insurer escapes liability because of the term in the policy. In this event the intermediary becomes liable… On the other hand, if an insurer does not draw attention to the clause, the insurer cannot rely on the clause as an exclusion in terms of the contract. In this event, the insurer does not escape liability because the other party did not know about the term, but the very opposite happens – he becomes liable in terms of his contract because the insurer cannot rely on the term… Applying this ruling to the current matter, Maduray could not be bound by a term she did not know about. Thus Renasa could not rely on the warranty to avoid liability and it then becomes liable in terms of its contract. If it is liable in terms of its contract, then clearly the broker cannot be liable. They are not jointly and severely liable but alternatively liable."

If these two determinations are taken as representative then it should be clear that the determinations are difficult to reconcile with rulings based on law and it is not surprising that when some of the leading determinations have been taken on appeal or review they have been overturned. What is surprising is the view of some of the Ombud's that their decisions should not be subject to scrutiny by the courts. It is clear that the appropriate role of the Ombuds will take some years to be worked out.

4.7.2 United Kingdom

Rawlings and Willett (1994: 311) note that the Insurance Ombudsman Bureau (I.O.B.), established as a voluntary scheme in 1981 as a response to the complexities and unfairness of insurance law, was based on a Memorandum and Articles of Association which received from "private individuals complaints or disputes over insurance policies issued in the United Kingdom, where the internal complaints mechanisms have been exhausted".

In England, the Financial Ombudsman Service has had the authority to investigate claims against insurance intermediaries since 2005. The Financial Services and Markets Act 2000 Section 228 (2) provides that the Ombudsman may determine a case by reference to what he perceives as "fair and reasonable in all circumstances of the case" implying that the law is not adhered to as strictly as it should be and the equity has a role to play in Ombudsmen's decisions.

5. PROFESSIONAL LIABILITY OF INTERMEDIARIES THROUGH CASES

Christensen (1990) and Ziomek and McCahill (1999) both suggest that there are several theories of liability under which an insurance intermediary may be liable:

1) Breach of contract – it must be established that a relationship had been created either by an express or implied contract. The insurance intermediary will be found liable for breach of contract if he has failed to comply with the duties imposed by the contract.

2) Breach of tort or negligence
    a. An alleged special relationship between the intermediary and the insured exists, Lord Atkin's neighbour principle - here the intermediary is alleged to be the agent of the insured or is held to the standard of care of a professional.
    b. Ordinary negligence – the intermediary is not considered to be a specialist. It is often alleged that the intermediary made negligent misrepresentations, omitted to advise the insured appropriately or failed to exercise proper skill, care and diligence in the performance of duties owed.
    c. Contributory negligence of the insured.

3) Breach of fiduciary duty – as a professional, the insurance intermediary owes a fiduciary duty to the insured to act in the best interests of the insured. Generally the proof of the existence of an express or implied contract is not required; it is only necessary to establish that the relationship involving the agent was one where fiduciary duties were owed.

4) Liability for fraud

Furthermore Richmond (2004) notes that insurance intermediaries may be sued by the insurers with whom they do business (this litigation will involve, amongst other things, claims by the insurer that the agent is obligated to indemnify the insurer in litigation with an insured), insureds, applicants for insurance, and sometimes third parties with whom they have had no obvious relationship.

Clarke (2000: 246) notes that insurance brokers are liable to their clients in both contract and tort for any failure to carry out their mandate with reasonable care and skill. Although it will almost always be the case that a broker will act on the basis of a written or oral contract with an insured, in which case an action will arise in contract for any breach of the broker's standard of care, a breach may also give rise to concurrent liabilities in negligence and under statute (Shub and Hopley; 2007: 4). The problem of the concurrency of actions, as previously discussed, means that the claimant could be free to pursue whichever cause of action will be most beneficial.

Ziomek and McCahill (1999) note that claims against insurance intermediaries will usually fall within the following categories:

i. Failure to procure insurance
ii. Failure to procure requested coverage
iii. Failure to procure adequate coverage
iv. Failure to advise
v. Failure to renew

A review of case law follows highlighting how the courts have dealt with the liability of intermediaries.

5.1 United Kingdom case law

- *McNealy v The Pennine Insurance Co. Ltd., West Lanc Insurance Brokers Ltd. and Carnell 1978* Lloyd's Law Review

McNealy had various jobs including a part-time job of being a guitar player for a band. In 1971 he bought a car which he wished to insure. He approached West Lanc Insurance Brokers in June 1971 where he dealt with a broker named Carnell who suggested he insure with the Pennine Insurance Company. The Pennine Insurance Company offered low rates to certain classes of motorists; however it excluded many classes of motorists from cover including, amongst others, full- or part-time musicians.

The broker, knowing of the exclusion, failed to mention these to McNealy, probably because he did not consider McNealy's part-time occupation. When a claim arose, the insurer repudiated the claim because of the wording which did not cover musicians. The court held that the broker was liable as the broker had a duty to see that the assured was properly covered. It should be noted that this was an unusual provision not generally found in insurance policies and the existence of this term was known to the broker and could not be known to the insured. Unless the broker advised the insured of this term, the insured would not know about it. This distinguishes the case from the failure to disclose material facts by the insured where these facts are known to the insured, not the broker.

- *General Accident Fire and Life Assurance Corporation and Others v Tanter and Others* 1985 2 Lloyd's Rep. 529

The prospective owner of a vessel, named the Zephyr, asked his insurance brokers to obtain quotes for suitable insurance. Insurance placed by the brokers on the London market covered normal marine perils and as most underwriters chose to reinsure all or part of the risk, the brokers further obtained a quote from the first defendant. The purchase of the vessel went ahead and the brokers were asked to place the insurance; they confirmed that all the insurance that had been requested was complete. Within a few weeks the vessel suffered damage due to adverse

weather conditions and was subsequently declared a total loss. The all risks underwriters were given notice and paid the ship owners.

The reinsurers however repudiated liability and claimed against the brokers in contract and tort alleging excessive liability under the reinsurance slip. The dispute arose in that the broker had arranged for insurance and reinsurance with two slips, one for 'All Risks' insurance with the insurers and the other for 'All Risks' reinsurance with the reinsurers. The reinsurers alleged that the broker had given them signing indications that their exposure would be limited. The court held that the brokers had acted negligently and were therefore liable to the reinsurers.

- *Forsikringsaktieselskapet Vesta v Butcher* 1985 2 Lloyd's Rep. 529

A Norwegian insurer, Vesta, placed reinsurance in the London market through brokers. The insured was a Norwegian fish farmer whose stock was destroyed in a storm. Vesta paid the claim but could not recover from its reinsurers because the insured had breached a warranty in the contract. Under English law the reinsurers denied indemnity. However under Norwegian law the insurers had to pay the insured's claim. Vesta then sued both the reinsurers and its brokers.

At first instance Vesta was successful against both the reinsurers and the brokers. It was held that the reinsurers breached the warranty in the reinsurance policy and that the brokers breached the contract (there was a contractual relationship as well as a duty of care between Vesta and the brokers).

- *Youell v Bland Welch & Co. Ltd.* 1990 2 Lloyd's Rep 431 - *(The "Superhulls Cover" case)*

Brokers were instructed to obtain reinsurance on the London market on behalf of insurers in respect of construction risk on three new buildings. The brokers informed the insurers that they had obtained the reinsurance as 'original' but in fact the reinsurance was subject to a cut-off clause, of which the brokers had failed to inform the insurers. The insurers would not have accepted the reinsurance had they known of that information.

The court held that the brokers were in breach of their duty of care both in contract and tort. The brokers were in breach of duty in failing to draft the contract wording with proper skill and care, in failing to inform the insurers of the nature of the insurance, and in failing to take the steps to provide extensions when the cover term expired. The court held that:

> "[the broker] must ascertain his client's needs by instruction or otherwise. He must use reasonable skill and care to procure the cover which his client has asked for, either expressly or by necessary implication. If he cannot obtain what is required, he must report in what respects he has failed and seek his client's alternative instructions."

- *Harvest Trucking Co. Ltd. v P B Davis t/a P B Davis Insurance Services* 1991 2 Lloyd's Rep 638 (QB)

This case held that a broker should advise its client of any onerous terms of the policy. Judge Diamond stated that:

> "… if the only insurance which the intermediary is able to obtain contains unusual, limiting or exempting provisions which, if they are not brought to the notice of the insured, may result in the policy not conforming to the client's reasonable and known requirements, the duty falling on the agent… may… entail that the intermediary should bring the existence of the limiting or exempting provisions to the express notice of the client, discuss the nature of the problem with him, and take reasonable steps either to obtain alternative insurance, if any is available, or alternatively to advise the client as to the best way of acting so that his business procedures conform to any requirements laid down by the policy…"

- *Prentis Donegan & Partners Ltd v Leeds & Leeds Inc.* 1998 1 Lloyd's Rep 326

The question of whether a Lloyd's placing broker who paid monies to underwriters in accordance with Section 53(1) of the Marine Insurance Act 1906 and had not been paid these

monies or commission by the assured or producing brokers could sue the producing broker was addressed.

The court held that the Lloyd's broker could claim from the producing broker stating that as there was no contract or privity of contract between the assured and the Lloyd's producing broker, the producing broker was liable for the unpaid monies.

- *FNCB Ltd. v Barnet Devanney (Harrow) Ltd.* 1999 EWCA Civ 1729

In 1989 the brokers, Barnet Devanney & Co. Ltd., arranged on behalf of First National Commercial Bank plc for the insurance of property with General Accident Fire and Life Association Corporation plc and others; the policy was effected in the names of the owner and the Bank. The property was destroyed by a fire in January 1991 and the insurers repudiated liability to both the owner and the Bank in June on the grounds of non-disclosure, misrepresentation, and breach of condition, only by the owner and not by the Bank.

In 1995 the Bank sought damages from the brokers for negligence and breach of contract. The broker was held liable for failing to obtain specific protection in the form of additional clauses in the policy.

- *Pangood Ltd. v Barclay Brown & Co. Ltd.* 1999 PNLR 678

Pangood owned a nightclub and instructed its broker, Barclay Brown, to obtain insurance for the premises against fire and other risks, who then instructed a placing broker to approach underwriters at Lloyd's to effect the insurance. The policy contained an 'auditorium warranty' that requires the policyholders to take particular measures to prevent a fire. A fire occurred and the underwriters refused cover alleging that the auditorium warranty had not been complied with. Pangood sued its brokers for not bringing the auditorium warranty to their attention and the brokers in turn sued the Lloyd's brokers alleging that they too owed a duty to bring the auditorium warranty to Pangoods attention.

The House of Lords held that the Lloyd's brokers did not owe a duty of care to Pangood in either contract or tort. Considering the negligence claim, the court held that the brokers instruction to the placing broker to obtain insurance did not involve an assumption of responsibility on the part of the placing broker to bring the auditorium warranty to the insured's attention.

- *J W Bollom & Co. Ltd. v Byas Mosley & Co.* 1999 Lloyd's Rep. PN 598

Brokers obtained insurance for Bollom against fire. However when a fire occurred the insurers repudiated the claim stating that a yard alarm was not switched on at the time of the fire, which was a condition of the policy. The insurers however agreed to a settlement of £5 million. Bollom then brought proceedings against its broker, Byas Mosley, alleging that it would have received a full recovery from the insurers if the brokers had not been negligent.

The court held that the brokers ought to have been aware of the clauses of the policy and informed the insured of such; thus the brokers had breached their duty to Bollom. This breach directly caused Bollom's loss.

- *Martin Elliott Johnstone v C & S Commercial Consultants* 1999 SLJ99/5783/2

The claim arose due to the insurance agent's failure to advise Johnstone that a policy effected on his behalf contained or might contain an 'auditorium clause', which provides that fire cover will not be effective under the policy unless the insured has emptied all ashtrays and removed the same from the premises each business day. When the Johnstone suffered a loss, the insurers repudiated liability on the grounds that the insured had breached the auditorium clause. The judge held that there was no duty on the agent to draw the insured's attention to the fact that the fire policy contained an auditorium clause.

- *Companhia de Seguros Imperio v Heath (REBX) Ltd.* 1999 EWHC 285 (Comm)

Companhia were insurers who had been used by the brokers as a front for the rest of the members of a pool. The insurer claimed damages from the brokers for breach of a written

binding authority agreements, claimed in tort for breach of fiduciary duties and also claimed negligent misrepresentation. The issue was whether the breach of fiduciary duties was statute-barred. It was held that provisions applicable to claims for breach of contract and tort applied to claims of breach of fiduciary duty; thus the claim was statute-barred.

- *Avon Insurance v Swire Fraser Ltd.* 2000 1 All E.R. (Comm.)

Avon were stop loss insurers who authorised brokers to issue stop loss policies on their behalf. Avon alleged that the brokers had misrepresented them and that, but for the misrepresentations, they would not have entered into the binding authorities and would not have had to pay the losses which they had suffered. The court however found that no misrepresentation had been proved.

- *George Barkes Ltd. v LFC Insurance Brokers* 2000 PNLR

The claimants instructed brokers to obtain insurance for their premises and contents. The brokers obtained a quote which the claimants accepted, however this policy did not cover 'extended theft'. When a theft occurred the insurers refused indemnity. The court held that the brokers were at fault as they should have drawn the claimants' attention to the fact that the policy did not cover extended theft.

- *Great North Eastern Railway (GNER) v Avon Insurance Plc* 2001 Civ 780

In 1998 GNER brought claims against its insurers, Avon, in respect of material damage and business interruption losses that resulted out of the derailment of one of GNER's trains, as a result of a defective wheel on a train due to faulty workmanship.

GNER had placed its business with Avon through Fenchurch Insurance Brokers since 1996. The policy wording for this cover included in its terms an exception for damage or consequential loss caused by "faulty or defective design, materials or workmanship, inherent vice, latent defect, gradual deterioration, wear and tear or frost".

In 1997 GNER changed their brokers to Jardine Insurance Services who renewed the cover with Avon on the basis of the original Fenchurch wording but no policy wording was issued on this renewal. In 1998 however Jardine published a market presentation document including the following narrower exclusion clause: "No cover is provided for damage or consequential loss caused by or consisting of faulty or defective workmanship, operational error or omission on the part of GNER or any employees, other than drivers and guards".

The derailment in 1998 of GNER's train was within the Fenchurch exception but not within the narrower Jardines exception. The court held that Jardines wording had never been officially agreed upon and thus the cover had continued on the basis of the Fenchurch wording. GNER appealed this decision; however the Court of Appeal held that the policy signed by Avon's underwriters upon renewal of the policy referred to the Fenchurch wording and not new Jardine wording put forward as this wording had not been discussed with Avon's underwriters. The court held that GNER's claim failed.

- *Aneco Reinsurance Underwriting Ltd. (in liquidation) v Johnson & Higgs Ltd.* 2001 UKHL 51

Brokers J&H invited Aneco to enter into a reinsurance treaty; Aneco told J&H it would only participate if it could obtain excess of loss reinsurance to protect its marine book, including its exposure on the Bullen Treaty. The brokers confirmed they could obtain such cover and placed the reinsurance. However J&H negligently misrepresented Aneco to the underwriters.

The Bullen treaty was a financial disaster with Aneco suffering losses of approximately $35million. Aneco claimed damages from J&H for breach of contractual duty of care and negligence in relation to the placement of the excess of loss reinsurance.

The brokers admitted liability to Aneco but claimed that the correct amount of the loss was the value of the reinsurance cover Aneco lost, i.e. $10million. However Aneco disagreed stating that

had the brokers made full disclosure Aneco would never have entered the reinsurance with Lloyd's at all and thus not suffered the loss of $30million.

The court found that in applying tort tests the brokers owed a duty of care, had breached that duty, and that Aneco had suffered a loss as a consequence of the breach. J&H however argued that its duty of care extended only to obtain the reinsurance and not to advise Aneco on what course of action to take; Evans LJ addresses this issue in the Court of Appeal:

> "… the fact that no reinsurance cover was available in the market is important because it introduces an additional head of breach of duty by [J&H]. They are liable not merely for failing to obtain effective cover on the terms which they reported to Aneco, but also for failing to report that no cover could be obtained. The last factor in particular means … that the Banque Bruxelles principle - compensating the claimant only for the consequences of the advice or information being wrong - fails to provide proper compensation in the present case. Aneco is also reasonably entitled to compensation for [J&H's] failure to report correctly the current market assessment of the reinsurance risks which Aneco was proposing to undertake. Those risks were central to Aneco's decision and Mr Forster took it upon himself to advise Mr Crawley with regard to them. This is far removed from the lender/valuer relationship and even from the client/professional adviser relationship to which the Banque Bruxelles case applies, and even more so from the doctor and mountaineer. … Aneco is entitled to recover damages for the whole of the losses which it suffered in consequence of entering into the Bullen Treaty, acting on [J&H's] advice with regard to the availability of reinsurance … and therefore on the current market assessment of the risk".

- *HIH Casualty & General Insurance Limited & Others v Chase Manhattan Bank & Others* 2001 Lloyd's Rep. 483

The insured, Chase, secured five film finance insurance policies with a broker, Heath, against the risk that the revenues from the films would be insufficient to repay the loan. Two films were placed facultatively and three by declarations off a line slip. There was subsequently a

substantial shortfall in the revenue and Chase claimed under the policies. The insurers repudiated the claims stating misrepresentation and non-disclosure, either fraudulently or negligently, by the broker. Chase however argued that a Truth of Statement clause in each policy waived the insurers' rights to rely on misrepresentation and non-disclosure. The Truth of Statement clause, as broken down by the court, read as follows:

> "[6] the insured will not have any duty or obligation to make any representation, warranty or disclosure of any nature, express or implied (such duty and obligation being expressly waived by the insured) and
> [7] shall have no liability of any nature to the insurers for any information provided by any other parties and
> [8] any such information provided by or non-disclosure by other parties including, but not limited to [Heaths]… shall not be a ground or grounds for avoidance of the insurers' obligations under the Policy or the cancellation thereof."

The Court of Appeal held that the clause waived any remedies the insurers had against Chase for Heath's negligence but did not waive the insurers' remedies if they could prove that Heath had acted fraudulently. Both parties then appealed to the House of Lords. It was held that phrase 6 relieved Chase of their obligations to make any disclosures but did not waive Heath's obligations as an agent. Furthermore phrase 7 and 8 excluded the insurers from seeking any remedy for the negligent actions of Heath.

The House of Lords further held that the clause did not cover liability for fraudulent misrepresentations by Heath stating that if a party wished to exclude liability for fraudulent misrepresentations of his agent then he must make use clear and unmistakable terms of such in the contract; the Truth of Statement clause did not constitute such a clause. Thus if the misrepresentations were made fraudulently by Heath, the insurers would be able to avoid the policy and claim damages in tort.

- *Alexander Forbes v SJB Ltd.* 2003 Lloyd's Rep. PN 137

Alexander Forbes effected Errors and Omissions (E&O) cover through SJB Ltd. The policy was a claims-made policy with standard requirements to notify claims, with the cover effected being separated from an umbrella policy for regulatory reasons. Alexander Forbes reported a complaint of pensions mis-selling to the brokers and in doing so discovered the potential for other such claims due to the Pensions Review obligations that were to be engaged. The brokers reported a single claim to the group insurer instead of to the professional indemnity underwriters. Furthermore the notification did not extend to the reporting of the risk of further claims. When it was identified that the wrong underwriter had been notified, a late notification was made to the correct insurer who agreed to cover the claim for mis-selling but refused to provide blanket notification for any further claims that may have arisen.

The court held that the brokers were negligent in failing to notify the correct insurer as well as not notifying the need for blanket notification. The judge held that a focused and deliberate approach should be required of the broker:

> "Brokers owe duties going beyond those of a post box. It was for the brokers to get a grip on the proposed notification, to appraise it and to ensure that the information was relayed to the right place, in the correct form. As the expert put it, they needed a strategy for handling claims..."

- *Goshawk Dedicated Ltd. & Ors v Tyser & Co. Ltd. & Anor* 2006 EWCA Civ 54

In the case of *Goshawk Dedicated Ltd. & Ors v Tyser & Co. Ltd. & Anor* in 2006 the English Court of Appeal held that brokers were obliged to make placing, claims and accounting documentation available to Lloyd's syndicates pursuant to an implied term of the insurance contract. Although this ruling was specific to the Lloyd's insurance market, it does however suggest that brokers may be obliged, due to an implied term in the contract itself, to provide underwriters with placing, claims and accounting documentation.

- *BP Plc v Aon Limited & Anor* 2006 1 All ER (Comm) 789

In *BP Plc v Aon Limited & Anor*, BP argued that a duty of care was owed by Aon; Aon denied the existence of any such duty in performance of brokerage services. The High Court held that as Aon had undertaken a responsibility to provide brokerage service to BP, these services ought to be provided with proper professional skill and care and failure to do so amount to breach of duty of care in tort. This ruling established that a sub-broker may owe a duty of care to an insured despite the absence of any contractual relationship however it fails to mention any principles of the duties of care owed by the broker to the insured.

- *HIH Casualty & General Insurance Limited v JLT Risk Service Solutions Limited* 2006 EWHC 485 (Comm)

Brokers who acted for both the insured and the reinsurer were found to owe a continuing post-placement duty to inform the reinsured of any potential coverage issues that may arise out of the breach of warranty in the original policy.

JLT had placed insurance cover to protect against the risk that three slates of films which had been financed would not generate sufficient revenue to repay the financing. HIH and others were the underwriters of this insurance. JLT further placed reinsurance with New Hampshire, Axa and others. JLT was the placing broker for both the insured and the reinsured.

The three slates of films were not successful resulting in HIH having to pay out under the three insurance contracts a total of US$ 54million. HIH then sought recovery from its reinsurers; however the reinsurers argued that a breach of warranty existed in the number of films to be made in each slate. The court held that such a breach did exist both in the insurance and reinsurance.

HIH consequently sought recovery from its brokers arguing that JLT was negligent in that they had not obtained agreement from the reinsurers to reduce the number of films making up the insured slates. JLT however argued that it had no such duty and that the loss suffered by HIH

was not caused by its negligence. At first instance the Commercial court held that JLT owed HIH a post-placement duty to inform than of any changes in coverage; JLT had breached this duty but this breach had not caused HIH's loss. Both HIH and JLT appealed this decision. The Court of Appeal ruled that JLT as brokers did owe HIH a duty to inform HIH of possible changes in coverage. JLT however did not face liability because the Court of Appeal found that JLT's breach of duty did not cause any loss to HIH.

- *Talbot Underwriting Ltd. v Nausch Hogan & Murray Inc.* 2006 EWCA Civ 889

In this case the matter of whether the shipyard constituted an 'additional assured' in terms of the shipbuilders' all risks policy of insurance and if the shipyard could enforce the policy as an undisclosed principal were addressed. Talbot was the underwriter in London and Nausch Hogan & Murray Inc. (NHM) was the insurance broker.

A contract had been placed with a shipyard by the owners of a ship for the completion of work to a vessel. NHM had been instructed by the ship owners to obtain a shipbuilders' all risks policy for the period of completion of the work on behalf of various parties including the shipyard as co-assured. Clause 15.12 of the policy read: "… which shall include [the shipyard] as an Additional Co-Assured and shall be endorsed to require the underwriters to waive any rights of recourse including in particular, subrogation rights against all Assureds thereunder…" NHM placed 40% of the risk with London underwriter Talbot, 35% in Norway and 25% in Russia; however the shipyard had not been named as co-assured in the London policy.

In October 2003 whilst still in the shipyard, the vessel sustained damage which was repaired by the shipyard that then claimed indemnity under the London policy. Talbot however rejected the claim on the grounds that the shipyard was not an insured. The shipyard then claimed against the ship owner and NHM for failing to procure the necessary insurance. The ship owners settled their claim and assigned their rights to Talbot who brought proceedings against NHM for breach of duty and negligence in placing insurance.

The following issues were raised:

- NHM argued that the shipyard fell within the 'additional assured' provision under the Conditions of the policy that provided: "Including Assured, interest of Mortgagees (and Notices of Assignment in respect thereof), Loss Payees, Additional Assured and Waivers of Subrogation as may be required" and as such the policy was extended to cover those persons with insurable interest.

  The judge however disagreed stating that the words 'as may be required' did not include any third party that the insurers had not agreed upon and that the words 'additional assured' referred to those parties that fell within the definition of the insured but did not exist at the time of cover.

- NHM then argued that the shipyard was an undisclosed principal.

  The judge found that there was no sufficient evidence to establish that inclusion of the shipyard in the policy.

- However if the shipyard was in fact insured as an undisclosed principal then there was no material non-disclosure of the ship owner's intention to contract on behalf of the shipyard.

  The judge held that disclosure was required of anything that would be deemed material and this included anything in relation to an undisclosed principal.

- NHM further argued that no loss had been by both the shipyard and the ship owners. It could be said that the damage was incurred due to the shipyard's negligence and that the ship owner was entitled to recover the full amount of the loss under the policy even though the shipyard had fixed the vessel at its own expense.

> The judge found that the loss had been suffered as a result of NHM's failure to include the shipyard as co-assured. The ship owners had sustained a loss (that is the chance to recover from its insurers under the insurance policy) as a result of NHM's breach.

- *Equitas Ltd. v Horace Holman & Company Ltd.* 2007 EWHC 903

Equitas are the assignee of the rights of most of the members of Lloyd's syndicates for the year 1992. Horace Holman & Company is a Lloyd's broker. The claim arose out of contracts of reinsurance written to protect Lloyd's syndicates. Equitas alleged that Horace Holman had breached their contractual, tortuous, and fiduciary duties. The Commercial Court held that brokers have a duty to take reasonable care to maintain proper and adequate records; in this case the brokers had a duty to have the correct accounts ready for their principals. The court further noted that the brokers had a fiduciary duty to provide Equitas with internal records that were related to the transactions undertaken by the brokers.

- *Arbory Group Ltd. v West Craven Insurance Services* 2007 QBD (Leeds)

West Craven had arranged business interruption cover for Arbory and several of its subsidiaries. A fire occurred and it was discovered that Arbory was substantially underinsured for business interruption due to West Craven's advice. The court held that the broker had a duty when arranging business interruption cover to ensure that the cover would enable the insured to recover to its pre-incident level of profitability. The judge held that:

> "… the duty of the broker in this case where business interruption cover was required was to effect such cover that would enable [Arbory]… to recover to its pre incident level of profitability; that the payment of such sum was, as the broker would appreciate, over and above any sums required to cover damage to a building and equipment; that in the circumstances of this type of cover, it was reasonably foreseeable that the failure to effect cover was liable adversely to affect profitability of the business so insured, if as a result of the broker's negligence insufficient business interruption insurance money was paid to

> enable the company to recover as it should have so recovered in the event that proper cover had been effected."

This case is believed to be the first of its kind, allowing an insured to successfully raise a claim for consequential loss as well as a claim for the recovery of the shortfall of insurance proceeds. This case is of significance to brokers as they may not only have a duty to calculate the correct sum insured for business interruption cover for the insured, but also may be required to advise the insured of the correct method of calculating that figure.

- *Fisk v Thornhill and Son* 2007 EWCA Civ 152

Fisk was a broker that had placed property insurance for the insured. He obtained a quotation for insurance through Thornhill; the policy was placed in the basis that the property was constructed of bricks, stone, slates and tiles, however the main part of the property was actually timber framed. Thornhill sent a renewal notice to Fisk who failed to mention that the policy was with the new insurers, CAN, and Fisk further obtained the insured's consent of the renewal. The property was damaged and CAN avoided liability on the grounds of breach of warranty. Fisk settled with the insured then sought contribution from Thornhill.

The judge at first instance dismissed Fisk's claim and Fisk thereafter appealed. The Court of Appeals held that as a sub-broker, Thornhill breached its duty to the insured in failing to bring the insured's attention to the new policy and as such Thornhill was to contribute 25% of the loss. This case highlights that sub-brokers also owe a duty to the insured to draw their attention to important terms of the policy.

- *Standard Life Assurance Ltd. v Oak Dedicated Ltd. and Others* 2008 EWHC 222 (Comm)

A claim by the assured, Standard Life Assurance (SLA), was brought against its underwriters, Oak, for the liabilities it incurred from the mis-selling of endowment policies. SLA brought a further claim against its brokers, Aon, for damages in respect of the amount it could not recover

from its underwriters. SLA alleged that Aon was in a breach of its duties in arranging the insurance.

It was held that Aon was in fact negligent in the placing of cover. A broker owes a duty to its client to identify and advise the client about the type and scope of cover required, and in doing so match the risk exposure of the business to the cover available. The judge set out an uncontroversial list of all the duties owed by insurance brokers, following the decisions in *FNCB v Barnet Devanney*[136] and *Talbot Underwriting v Nausch Hogan & Murray*[137], although only the second duty applied to the case at hand:

- To advise the insured of the type and scope of insurance needed
- To arrange cover that meets those requirements
- If such cover is available, to ensure that all exclusions are made clear to the insured
- In preparing the policy, to ensure the language used fits the insured's needs
- To act with the same standard of care upon renewal of a policy as with the original policy

This case highlights the potential liabilities faced by brokers by the careless use of wording and language in policy documents.

5.2 South African case law

Until recently South African cases involving intermediaries have been rare indeed.

- *A.W. Cowey v London and Lancashire Fire Assurance Company* 1899 20 NLR 90

One of the earliest examples of the duty of an insurance intermediary to advise a client can be seen in *A.W. Cowey v London and Lancashire Fire Assurance Company* 1899 20 NLR 90. Here the insured brought an action to recover a sum of £500 under a policy of insurance with the defendant company.

[136] *FNCB Ltd. v Barnet Devanney (Harrow) Ltd.* 1999 EWCA Civ 1729
[137] *Talbot Underwriting Ltd. v Nausch Hogan & Murray Inc*. 2006 EWCA Civ 889

Cowey had a store at 457 West Street Durban and a dwelling house at 124 West Street. A policy of insurance was effected with London and Lancashire Fire Assurance Company against fire for £500 for the furniture at 124 West Street, which was renewed each year by the payment of annual premiums. In 1895 he moved the furniture from 124 West Street to 457 West Street. The premise's at 457 West Street was destroyed by a fire in July 1898. One of the conditions of the policy stated to the following effect:

> If, after the insurance has been effected, anything whereby the danger of loss or damage to any of the property insured is increased be done thereto, or to or upon or in any building or place in which any of the said property is contained, or if any property thereby insured be removed from the buildings or place in which it was therein described as being contained or if any of the within mentioned premises become vacant or unoccupied for more than 30 days, or if any addition to the risk arise from any other source whatsoever, without in each and every of such cases the assent or sanction of the Company signified by endorsement thereon, or if the insured should refuse or neglect to pay any further premium which may be demanded in consequence of any increase of risk, the insurance as to the property affected thereby shall cease to attach.

Shortly after moving the furniture, the agent, Mr. Sinclair, called Cowey at the store; Cowey enquired as to when the next premium was due. The agent said "there?" but Cowey replied "no here" and made a gesture to indicate the store. The agent admitted that at the time he was aware that the furniture had been moved but this fact later slipped his mind. The agent sent out notices for the premium but did not increase it as it should have been due to the character of the building at 457 West Street. Cowey claimed £500 from the insurer who repudiated on the grounds that the removal of the furniture to 457 West Street had not been notified to the insurer within the terms of the policy.

The judges in this case were of differing opinions as to the liability of the intermediary. However, the majority of the Bench did not believe that Mr. Sinclair understood from the casual conversation which took place between himself and Cowey that the insured goods had been removed from one store to another and thus could not be held liable for the loss.

- *Schneider v Karroo Board of Executors* 1923 AD 131

The earliest case involving the placement of insurance which could be found was in 1923, but strictly speaking ut did not involve an insurance intermediary in the modern sense.

The first professional liability case to be brought against an insurance intermediary in South Africa dates back to 1923; this is the case of *Schneider v Karroo Board of Executors*.

The facts of the case are as follows: Gertie Cohen conducted a business, trading as Cohen & Co, in which Schneider had an interest. In October 1920, Schneider gave the general manager of the defendant company, Kirk, power of attorney for the protection of his interests in the business and instructed him to insure the stock of the business. Kirk undertook to procure the insurance with Union and National Company; Schneider signed a proposal form for which the defendant company were agents. Kirk forwarded this proposal to the company who however refused it. Kirk informed Cohen of the refusal and that is was unlikely that another company would accept the proposal as his company had refused it and that it would be wiser to put the business in a better financial position and then try with the same company again. Kirk did not however inform Schneider of the refusal, reasoning that Schneider and Cohen's interests were one in the same with regard to the insurance and that he and Cohen had decided on the wisest course of action.

The court held that up to this point there had been no negligence on part of Kirk in failing to carry out his mandate. He had endeavored to procure insurance for the stock and subsequent to the refusal of the proposal by Union and National Company, had taken the wisest course of action. His failure to inform Schneider of the refusal was not a ground for action.

Schneider visited the business in December 1920 whereupon he was informed by Kirk that the insurance had not been effected and that Kirk hoped that the application might be renewed; Schneider thus again instructed Kirk to insure the stock, which he again undertook to do. Thereafter Kirk, in breach of his duty to procure the insurance, permitted, without Schneider's authority, the husband of Gertie Cohen to insure the stock with General Company. Kirk further

breached his duty in neglecting to ensure that Cohen answered the questions of the proposal form correctly, specifically the question:

> "has any proposal for insurance made by you or any member of your firm been declined by any insurance company?"

To this question Cohen answered "No", which was clearly incorrect; the previous declinature of insurance was a material fact.

On the 18th of February 1921 the stock was burnt by a fire; the insurer repudiated liability due to the incorrect answer on the proposal form and thus Schneider suffered £3000 in damages. Schneider claimed damages from the defendant company on the following grounds:

- Kirk failed and neglected to effect the insurance but allowed Cohen to do so without any authority;
- Kirk neglected to ascertain and ensure that Cohen answered the questions in the proposal form correctly;
- Kirk assured Schneider at the end of January that everything was in order with reference to the insurance.

With regard to the first ground J.A. Juta held that given Cohen's position in the firm, he was entitled to insure the stock and did not require the consent or permission of Kirk. Juta was of the same opinion with regard to the second ground, that it could not be attributed as negligence on part of Kirk for the failings of Cohen to correctly answer the questions in the proposal form; Cohen was fully competent and informed of the matter relating to the previous refusal of insurance. With regard to the last point, Juta held that it is not clear what ground this is made a cause of action even if the allegation be true; Kirk did not know that Cohen had given an incorrect answer, all he knew was that a cover note had been issued and the premium paid so he may have been truthful when he stated that the insurance was in order.

The Cape Provincial Division ruled in favour of the defendant company, and on appeal, the Appellate Division affirmed this decision holding that there was no breach of duty on part of the intermediary towards Schneider.

- *Rabinowitz and another NNO v Ned-Equity Insurance Co. Ltd. and another* 1980 1 403 W

This case, again strictly speaking, did not involve an insurance broker, but the court found it necessary to mention brokers and hence it is of interest. An argument arose as to whether or not the insured had made certain statements in the proposal form. It was argued on behalf of the insured that the broker and not the insured had filled in the proposal form and hence the insured could not be held to the statements in the proposal form. Justice Nicholas response to this was:

> "…I am satisfied that the deceased [the insured] was bound by the statements [by the broker] as fully as if he had signed it [the proposal] himself"

For a discussion on this case consult Advocate (1980) and Havenga (2001: 19 et seq).

- *Stander v Raubenheimer* 1996 SA 670 O

The case of *Stander v Raubenheimer* in 1996 was, up until recently, thought to be the first professional indemnity case brought against an insurance intermediary. The facts are as follows: Stander built a new house in 1988 and telephoned his broker, Raubenheimer, to inform the insurer; the information was passed on and the insurance was renewed. A fire occurred in 1990 destroying the house and its contents and it was at this point that it was discovered that the house had a thatched roof. The insurer repudiated the claim on non-disclosure, however it made an ex-gratia settlement of R30 000. Stander then sued his broker for the difference of the settlement and the loss; he alleged that the broker should have asked what material the roof was made of. The trial court ruled in favour of the broker. However, on appeal, the broker was held liable with

the court relying on the English case of *McNealy v Pennine Insurance.*[138] The finding was in part influenced on specific evidence led in the case that that broker had agreed that insurance would be obtained to ensure that the insured was at all times covered against damage if that cover was available.

Vivian (1996) notes that in this case no reference is made either to South African law of agency or to Roman law of mandate and furthermore there is no mention of the relevant home owner's policy which gives rise to the question: was the insured aware that the type of construction was material and mentioned it in terms of one policy and not the other? The law places the duty to disclose on the insured to make all material disclosures, not the intermediary; however the judgment in this case implies that it is the brokers' duty to ask.

- *Jowell v Bramwell-Jones and others* 2000 (3) SA 274 SCA

The case of *Jowell v Bramwell-Jones and others* in 1998 and subsequently on appeal in 2000 included, amongst other claims, a claim for advice wrongfully given to a trustee. Here the late Dr. Alan Jowell made provision in his will for the establishment of a trust where his wife was the income beneficiary as well as the nominated trustee and his four children would be the capital beneficiaries on the death of his wife. In 1989 Mrs. Jowell emigrated to Canada where she wished to maximize her income and have this income remitted to Canada. As she lacked the knowledge and ability to conduct such a transaction she hired the defendants (a significant number of professional persons) who professed to have the expertise in such matters, and for a reward would advise her to lawfully achieve her objectives. The future beneficiaries, the appellant alleged that in advising and assisting Mrs. Jowell to maximize her income, the capital benefit had diminished and accordingly he would suffer a substantial loss. The appellant alleged that the defendants' conduct was wrongful and that they intentionally and deliberately, alternatively negligently, violated the rights of the capital beneficiaries. Scott JA held that the appellant's action was premature since Mrs. Jowell was still alive and the measure of the loss could not be determined until the capital benefits became due i.e. on the death of Mrs. Jowell.

[138] *McNealy v Pennine Insurance Co. Ltd., West Lanc Insurance Brokers Ltd. and Carnell* 1978 Lloyd's Law Review

The SCA accordingly upheld the second exception by the Court *a quo* holding that the action was premature. It should be noted that this case involves a claim for pure financial loss and only became possible because of the recognition of claims of this nature.

- *Ries v Boland Bank Ltd. and another* 2000 4 SA 955 C

A case against a broker involving long-term insurance arising out of the failure to change the beneficiary of the policy occurred in *Ries v Boland Bank Ltd. and another*. The court ruled in favour of Mrs. Ries holding that the broker should have made more of an effort to get Mr. Ries to complete the necessary forms, and because he took no such steps he was negligent. Mr. Ries died before completing the forms. The broker had advised both Mr. and Mrs. Ries that until such time as the forms were completed no change of beneficiary would take place. Despite this Mr. Ries did not complete the forms.

Vivian (2001) notes that this case is unprecedented in the history of South African law and suggests that this case would have been unsustainable in the past because the common law did not recognize liability for either omissions or pure economic losses and that the common law provided indemnification for damages, not creating additional assets.

In the *Ries* case the broker was accused of omitting to do something which he should have done; his actions did not cause the loss. It should be noted that as a general rule the law of negligence does not impose a duty of care in respect of the failure to act and furthermore under Roman-Dutch law there is no liability for mere omissions. The judgment in this case thus highlights a significant problem in the law: the basis of liability is in essence at the discretion of the judge. Aristotle famously stated that the law is reason free from passion; however the basic rule of law is violated when liability is imposed at the discretion of judges.

The Supreme Court of Appeal overturned the decision of the *Ries* case in the appeal case of *BoE Bank Ltd. v Ries* (BoE Bank took over Boland Bank). The High Court judge Erasmus AJ drew an analogy between a broker who does not change beneficiaries and an attorney who negligently draws up a will in his conclusion of the brokers' liability. The Supreme Court of Appeal rejected

this approach of law by analogy and thus overturned the decision of the High Court. The court also rejected the idea that brokers and attorneys are analogous. This decision brought the South African law closer to that of the English and American law of torts.

- *Lenaerts v JSN Motors (Pty) Ltd. and another* 2001 (4) SA 1100 (W)

In *Lenaerts v JSN Motors (Pty) Ltd. and anothe*r the plaintiff insured his vehicle through a system operated by a broker. The policy contained a territorial exclusion which excluded cover if the vehicle was driven in Zambia. The plaintiff was involved in an accident whilst driving in Zambia where his vehicle was severely damaged. On return to South Africa he submitted a claim which was rejected because of the territorial exclusion. The broker had not made the plaintiff aware that a territorial exclusion existed. The plaintiff sued the broker both in contract and delict. Lenaerts alleged that the broker breached its obligations to act with reasonable care, skill, and diligence.

In the execution of the mandate on behalf of the insured, the insurance broker owes the insured a duty of reasonable skill and care. This duty includes the duty to take reasonable steps to collect and convey material information to and from the insured. It was held that the territorial exclusion was a material exclusion and thus it was the brokers' duty to inform Lenaerts of the exclusion as stated by Potgieter AJ relying on the English cases of *McNealy v The Pennine Insurance Co. Ltd*[139]. and *Harvest Trucking Co. Ltd. v P B Davis t/a P B Davis Insurance Services*[140]:

> "I consider that in our law, as in English law, the duty to exercise reasonable care and skill in appropriate cases extends to the duty to take reasonable steps to elicit and convey material information both from and to the insured. This includes information about the terms of the policy which, if contravened, might leave the insured without cover. It is part and parcel of the broker's general duty to use reasonable care to see that the insured is covered".

[139] *McNealy v Pennine Insurance Co. Ltd., West Lanc Insurance Brokers Ltd. and Carnell* 1978 Lloyd's Law Review

[140] *Harvest Trucking Co. Ltd. v P B Davis t/a P B Davis Insurance Services* 1991 2 Lloyd's Rep 638 (QB)

The proposal further contained a clause for the limitation of liability in favour of the broker which stated that:

> "I hereby accept and acknowledge that, in the event of the non-acceptance of this proposal by the underwriters concerned, or in the event of a repudiation of a claim by the underwriters, the insurance brokers will not in any way be liable for any claim of whatever nature which I have or in the future may have in respect of the insurance of my vehicle"

The court found that the exclusion exempted the broker from liability for any claim which may arise in respect of the contract of insurance but did not exempt the broker from a claim due to the breach of agreement by the broker to perform its duty under the brokerage contract. The court found the clause ambiguous and thus interpreted it against its author so as not to exclude liability.

It can thus be said that in South Africa a broker has a duty to inform the insured about contract terms, especially exclusions.

- *Lappeman Diamond Cutting Works (Pty.) Ltd. v MIB Group (Pty.) Ltd. and Glenrand MIB Ltd.* 2003 4 ALL SA 317 (SCA)

This very long running case dealt with the extent of the specialist broker's duty to advise the insured of the implications of an onerous term in the insurance policy, which required detailed records to be kept of the insured diamonds. Lappeman instituted a claim against the brokers, MIB Group, alleging that damages had been sustained as a result of MIB Group's breach of contract, alternatively, negligent performance of a duty.

The crucial provision in the policy upon which the underwriters avoided liability was clause (b) of the Specific Conditions, which Plewman J found to be a promissory warranty, read:

> "It is understood and agreed that the Assured shall keep detailed records of all sales, purchases and other transactions and that such records shall be available for inspection by the Underwriters or their Representatives in case of a claim being made under this Insurance Certificate."

After the loss of the diamonds it appeared that the records had not been kept leading to the repudiation of the claim. Lappeman alleged that MIB Group had failed to mention this provision to him. In essence that the broker had breached his duty to inform the insured of the policy terms. Lappeman further alleged the broker did not familiarize themselves with his business and were therefore in breach of their duties. The trial court found that MIB Group was not liable for the breach of duty; the High Court, on appeal, concurred accepting that the broker had indeed informed the insured of the policy term. This decision signifies that a broker cannot be expected to control the business of the insured and that his duty does not extend so far as to ensure that the insured complies with his obligations under the policy. The specialist broker's duty is discharged once he has drawn the attention of the insured to the obligations of the policy but does not require him to ensure that the insured complies with these obligations.

- *BPC Insurance Brokers (Pty.) Ltd. v Schultz* SCA case no: 438/2002

The broker was alleged to have breached his contractual obligations that he owed a duty of care to the insured by not informing the insured that he was required to report a claim with the police upon an accident. The court of the instance held the broker liable to the insured.

- *Mutual and Federal Insurance Co. Ltd. v Ingram No and others* 2009 (6) SA 53 (E)

Ingram suffered a significant loss when a portion of the wall of a car dealership collapsed inwards, causing extensive damage to a number of vehicles in the showroom. An insurance broker lodged a claim on behalf of Ingram in respect of the loss suffered. The insurer, Mutual and Federal, however repudiated liability on the basis of a specific exception to liability in the policy which stated that "the company will not be liable under this subsection for damage to

vehicles… whilst in or on the premises if the loss or damage is caused by or arises directly or indirectly from… weather conditions."

An action was instituted against the insurer and the broker in the alternative on the basis that if the insurer was not liable then the broker had breached its duty to provide comprehensive coverage.

The High Court held that the insurer had failed to prove that it was exempt from liability. On appeal to the Eastern Cape High Court however, an expert witness proved that the damage sustained fell within the specific terms of the exemption of the policy, and the insurer was thus exempt from liability.

On the claim against the broker, the court held that a broker has a duty to exercise reasonable care and skill to obtain and convey material information to and from the insured, and it is part of a broker's general duty to the insured to ensure that the insured is adequately covered. It was held that the broker negligently breached his duties and was thus held liable for compensation for the loss suffered.

- Ombud determinations

It is emphasized that this section examines a growing number of cases which have been heard in the courts involving intermediaries but it must be remembered that in addition to these there is an even longer and growing list of determinations made against intermediaries by the Ombud. As pointed out, how these will be reconciled will be a matter of concern in the years to come.

5.3 Australian case law

- *Odgen v Reliance Vice Brinker Company Pty. Ltd.* 1973 2 NSWLR 7

The insured had various claims under a products liability policy with Royal & Sun Alliance who denied renewal of the policy. The broker arranged alternative cover but failed to disclose to the

new insurer the insured's claims history. Upon the filing of a claim the new insurers denied liability on the basis of misrepresentation and non-disclosure. The court held that the broker owed a duty to exercise reasonable skill and care in the discharging of obligations and was thus liable.

- *Fanhaven v Bain Dawes Northern Pty. Ltd.* 1982 2 NSWLR 57

The court stated that a broker had an obligation to procure suitable policies for its clients in relation to their risks and give the client advice. The court held that:

> "Insurance brokers are agents who make it their business to procure contracts of insurance for those who employ them. Having undertaken to obtain insurance an insurance broker must exercise proper care and skill in carrying out the assured's instructions… I have no difficulty in seeing that this involved it in procuring suitable policies of insurance to protect its client against relevant risks of loss, advising of options and pointing out reasons for differential premiums. In these senses it became an insurance advisor."

- *Mytor Investments Pty. Ltd. v General Accident Fire and Life Insurance Corporation* 1984 3 ANZ

Mytor instructed a broker to arrange cover for the possibility that water rising from an inlet would flood a hotel. Following a cyclone the hotel was flooded. The policy however included an exclusion clause which excluded loss and damage caused directly or indirectly from the sea. It was held that the broker breached his duty of care in obtaining appropriate coverage for the insured.

- *Norwest Refrigeration Services Pty. Limited v Bain Dawes (W.A.) Pty. Limited and Geraldton Fisherman's Co-Operative Limited* 1984 A.L.J.R. 521

Norwest owned a fishing vessel which was insured through a fleet policy arranged by the Co-operative. The proposal form was completed by a representative of Norwest, handed over to the

Co-op, and then to Bain Dawes who organised with the underwriters to have the vessel added to the fleet policy. The policy contained an exclusion of liability for vessels that did not have a current certificate of survey issued pursuant to Western Australian legislation. Both the Co-op and Bain Dawes were aware of this exclusion but failed to mention it to Norwest.

The vessel was subsequently destroyed by a fire and the underwriters escaped liability relying on the exclusion clause. The judge dismissed the charges against the Co-op and Bain Dawes stating that neither knew nor ought to have known of the certificate of survey. Norwest appealed the decision to the Supreme Court of Western Australia, which dismissed the appeal against Bain Dawes allowing the appeal against the Co-op. It was held that the Co-op failed to take reasonable care in allocating appropriate insurance coverage to Norwest and was thus liable. The court stated that the Co-op had a duty to warn Norwest of the exclusions within the policy regardless of whether the Co-op knew or ought to have known of the survey certificate.

- *Eagle Star Insurance Company Limited v National Westminster Finance Australia Limited & Others* 1985 3 ANZ

This case established that a broker is under a duty to use reasonable skill and care when seeking to obtain coverage for his clients. The court held that it was the broker's duty to use reasonable skill and care in obtaining cover in a specific geographical location chosen by the insured.

- *Brooks v Sirius Insurance* 1985 3 ANZ

A broker arranged a 30 day cover note for the insured's truck. The broker, relying on information about the insured from a third party, who contacted the broker on the insured's behalf, provided the insurer with incorrect information. The truck was damaged however and the insurer refused to pay to claim. The insured successfully sued the broker for negligence in failing to take reasonable care when obtaining information about the insured.

- *Provincial Insurance Australia Pty. Ltd. v Consolidated Wood Products Pty. Ltd.* 1991 25 NSWLR

The insured contacted a broker to arrange insurance against various risks including property damage and loss of profits, stating specifically that a policy that would cover all circumstances of water entering the property was required. The broker obliged and arranged two policies with the insurer. The property was subsequently flooded and the insurer denied liability due to an exclusion clause.

It was held that the insurer was not liable and that the broker was negligent as he owed a duty to the insured to exercise proper skill and care. This highlights the importance of the broker going through the list of exceptions in the policy with the insured.

- *Brooklyn Lane Pty. Ltd. v MIC Australia Pty. Ltd.* 2000 VSC 33

In June 1995 Brooklyn Lane's premises were destroyed by a fire; the insurer denied liability for the loss of accounts receivable but had previously paid a settlement of $225 000 for separately insured property destroyed in the fire. Brooklyn Lane then sued its insurance broker, MIC, for breach of contract and breach of duty of care in tort for the difference of the amount it had received from its insurers and the amount it would have received had the broker arranged the correct coverage. The issue was whether the broker was liable because he had failed to obtain cover for loss of accounts receivable.

The judge found that Brooklyn Lane had not given the broker instructions to obtain cover for loss of accounts receivable and thus the claim was dismissed.

- *Elilade Pty. Ltd. v Nonpareil Pty. Ltd. & CIC Insurance Limited* 2002 FCA 909

Elilade's stock and plant was damaged when water had flowed onto its premises after a severe tropical rainstorm. Elilade brought a claim against both its insurer, CIC, and its broker, Nonpareil; the former for wrongfully declining indemnity under the insurance policy and the

latter for failing to exercise reasonable care in contract and tort by not having advised Elilade of the availability of flood insurance.

Justice Mansfield held that in order for Nonpareil to discharge its duty of care it was required to expressly raise the issue of flood insurance with Elilade and make it aware that flood was excluded from the defined events under the policy. He further found that Nonpareil had failed to discharge this duty to Elilade and that even if Elilade had been properly informed they would not have instructed the broker to secure flood cover; thus the brokers' breach of duty did not cause Elilade's loss and Elilade's claim failed.

This case highlights the importance of a broker to fully inform their clients in order for them to make informed decisions.

- *Tanevski v Trenwick International Limited* 2003 NSWCA 303

This decision of the New South Wales Court of Appeal highlights the relationship between the insurer and the agent. The issue involved whether the insured was covered under the policy and if so, who was the insurer. Judge Davies held that:

> "In my opinion, when a party seeks insurance from a broker and that broker, having the authority of an insurer, binds the insurer in favour of the party seeking insurance, a contract between the insurer and the insured will ordinarily come into force, notwithstanding that the broker may have breached the instructions which the insured party gave. Here, there was an insurance contract and consideration given by the insured to the insurer."

The decision of this case shows that an insurer may still face liability even if the agent issues a certificate showing a different insurer and may affect the way the agency relationship operates.

- *Dickinson v National Mutual Life Association of Australia Ltd. (trading as AXA Australia)* 2003 VSC 325

Dickinson, a chiropractor, instituted proceedings in the Supreme Court of Victoria, against his insurer, AXA Australia, who denied liability. The insurer used a defence of fraudulent non-disclosure and issued third party proceedings against the agent alleging that the agent breached his obligations to exercise reasonable skill and care when assisting the insured in completing the application forms; in terms of the agency agreement, the agent is expected to discharge his duties with reasonable skill and care and further owes the insurer a common law duty of care in carrying out his duties.

Smith J found that the insurer had instituted the claim against the agent due to loss of opportunity to impose an exclusion and that there was only a 20% probability of the insurer using the opportunity to impose that exclusion. He held that further submissions from the parties would be necessary to compare the liability of the insurer. The decision shows that agents who are negligent or breach their agency duties may be held separately liable for the insurer's loss of opportunity to impose policy exclusions.

- *Tosich v Tasman Investment Management Ltd.* 2008 FCA 377

Tasman Investment Management Limited, a financial planning firm, advised its clients, including Mr. Tosich, of a new investment opportunity. The project failed and Tosich sued Tasman for his losses. Through its broker, AON Risk Services, Tasman had entered into an 'Investment Managers Insurance Policy' with American Home Assurance Company (AIG). AIG rejected Tasman's claim against the policy who then cross-claimed against AIG for indemnity relating to the claims arising from the failure of the project, and secondly against AON for failing to procure adequate coverage if the claim against AIG failed. Tasman alleged that AON as its broker did not take all reasonable steps to procure cover against liabilities incurred as a financial planner. The court held that Tasman was liable to Tosich and further that Tasman's claim against AIG fell outside the required definition.

5.4 New Zealand case law

- *Parkinson v National Insurance Company of NZ Limited* 1991 6 ANZ

The insured gave the broker instructions to arrange cover; however the broker only sought this cover five days later. The court found that the broker was liable because he did not act within a reasonable time; the normal business practice would be to arrange cover immediately with the insurer.

5.5 United States case law

In the United States, each individual State adheres to its own rule of law, thus the case law varies from State to State.

5.5.1 California

- *Jones v Grewe* 1987 189 Cal.App.3d 950

The Second Appellate District held that an insurance broker owes a duty to procure the insurance requested by the insured with reasonable care and diligence but that this relationship does not impose a duty on the broker to advise the insured on specific matters. The court stated that:

> "The general duty of reasonable care which an insurance agent owes his client does not include the obligation to procure a policy affording the client complete liability protection… An insurance policy arises out of the insured's desire to be protected in a particular manner against a specific kind of obligation. It is the insured's responsibility to advise the agent of the insurance he wants… Ordinarily, the person seeking liability insurance knows better than the insurance agent the extent of his personal assets and the premium he can afford or is willing to pay."

- *Century Surety Co. v Crosby Insurance Inc.* 2004 124 Cal.App.4th 116

The insurer claimed that the broker had misstated information on the insured's application form and had defended the insured until it learned of this misrepresentation. The insured sued the insurer for breach of contract and bad faith, who then cross-complained against the broker for damages for fraud, negligent misrepresentation and common law negligence. The trial court dismissed the cross-complaint against the broker stating that the broker did not owe a duty of reasonable care to the insurer.

The Court of Appeal reversed the decision of the trial court stating that it would be unreasonable if the law did not allow the insurer a remedy against the broker. The court held that insurance brokers owe a duty to exercise reasonable skill and care when preparing insurance applications, the breach of which may result in the broker being held liable not only to the insured for fraud but to the insurer for negligence and further stated that:

> "[It] should not be construed as treating an insurance broker as a guarantor of information in an insurance application or as imposing a duty on the broker to independently investigate information provided by the insured. However, when the broker knows of actual misstatements, the broker may be held liable for transmitting those misrepresentations in an insurance application knowing the insurer will reasonably rely on them."

This decision of the Californian Appeal Court changed the long-established law and altered the way in which the relationship between broker, insured, and insurer was dealt.

- *Third Eye Blind Inc. v Near North Entertainment Insurance Services LLC* 2005 127 Cal.App.4th 1311

A band, Third Eye Blind, employed the services of a broker, Near North, to obtain a commercial general liability policy for the group. The policy obtained however contained an exclusion for

personal injury and advertising injury under a "Field of Entertainment Limitation Endorsement (FELE)".

When the band was sued by a former member, the insurer denied coverage on the basis of the policy exclusion. The band then sued the insurer for breach of contract and the broker for negligence and breach of contract in failing to give appropriate advice to the band. The insured obtained a favourable ruling against the insurer and settled the claim but the broker contended that he could not be liable since the trial court found that the policy provided coverage. The court however disagreed and held that the broker should have advised the insured for the potential gap in coverage; the insurer's denial of coverage, regardless of whether it was wrongful, was a foreseeable harm which could have been avoided. A broker can thus be held liable for negligence even though the insured obtains coverage from the insurer.

The decision of this case is in direct conflict with earlier cases regarding duty of care as it implies that the broker is effectively the insured's guarantor should the insurer deny cover.

- *Business to Business Markets Inc. v Zurich Specialties* 2005 135 Cal.App.4th 165

The insured, Business to Business, hired an Indian software company, Tricon, to write a computer program. The contract stipulated that Tricon carry an Errors & Omissions policy to compensate the insured should they fail to produce the software. The broker contacted a surplus lines broker and placed the policy. The policy excluded coverage for claims arising from or related to work performed in India.

Tricon failed to deliver the software and the insured sued for breach of contract. The insurers refused to pay the claim on the grounds of the policy exclusion. The insured also sued the broker for negligence. The brokers however claimed that they owed no duty to the insured as they had had no direct dealings or contact with the insured. The court held that brokers owe a legal duty of care to a third party even though the insurer refused to pay the claim.

The decision of this case thus extends the potential liability of brokers to allow third parties who have had no relationship with the broker to seek redress from the broker.

5.5.2 Florida

- *Toomey v Wachovia Insurance Services Inc. G* 2006 450 F3d 1225

Toomey and Holman were employees of IMC, a mortgage based business; Wachovia was IMC's insurance broker. In 1997 IMC purchased Toomey and Holman's mortgage business appointing them officers of the subsidiary and providing them with five-year employment plans. IMC, under financial pressure, ceased operations of the subsidiary and notified Toomey and Holman of the termination of their contracts. Toomey and Holman then successfully sued IMC in the United States District Court for the District of Maryland for being terminated without cause for $1.8 million.

When IMC initiated settlement negotiations it discovered it had lost the policy's coverage for breach of employment contract claims. IMC had extended this coverage with Wachovia for several months as it knew that the coverage was due to expire during the litigation with Toomey and Holman. It was alleged that Wachovia had removed the coverage without IMC's knowledge. IMC executed a settlement with Toomey and Holman to the effect that for $1.5 million they would dismiss all charges against IMC except those for the breach of their employment contracts. IMC further agreed to assign all its rights including its causes of action to secure indemnification for the $1.8 million judgment.

Toomey and Holman then instituted charges against Wachovia alleging that Wachovia had breached its duties owed to IMC, that Wachovia was negligent in its dealings with IMC, that Wachovia had intentionally interfered with their rights under the employment contracts, and that Wachovia had breached its duty directly to them. The district court granted Wachovia judgment as a matter of law on all claims except the assigned claim of breach of fiduciary duties owed to IMC on which a jury gave a verdict of $1 069 200 in favour of Toomey and Holman. Wachovia

appealed this decision and Toomey and Holman cross-appealed. The Eleventh Circuit Court provided the following questions for determination under Florida law:

(i) What is the effect of a settlement agreement between two parties that explicitly contains both an assignment of causes of action against a third party insurer and an immediate release of the insured on the same causes of action?

(ii) Can a claim for breach of fiduciary duty against an insurance broker be assigned?

5.5.3 Georgia

- *Westchester Specialty Ins. Services Inc. v U.S. Fire Ins. Co.* 1997 119 F.3d 1505

The federal appeals court, when applying Georgian law, stated that the insured's failure to read the policy, if he had a copy of the policy in his possession, would exempt the broker from any liability that may be due to the alleged negligent procurement of insurance coverage. An exemption to this general rule under Georgian law was however put forward by the court: where the broker acts as an expert and the insured relies on the brokers' expert advice even, the broker may be held liable in situations of alleged negligent procurement of coverage, even though the insured had a copy of the policy and failed to read it. However, even in this situation, if it is apparent upon analysing the policy that the insured would have discovered that the broker failed to procure adequate insurance, then the broker, acting as an expert, may escape liability.

5.5.4 Indiana

- *Westfield Insurance Company v Yaste, Zent & Rye Agency* 2004 Ind. Ct. App. 806 N.E.2d 25

Westfield claimed damages from Yaste, Zent & Rye Agency ('Agency') alleging that the Agency was negligent and made fraudulent misrepresentations to it. The trial court granted a summary judgment in favour of Agency. Westfield appealed this decision arguing that Agency owed them a duty to act honestly and with due diligence, a duty which they breached. Westfield

further asserted that Agency had a duty to inspect an amended policy received from Westfield, also breaching this duty. Westfield thus suffered damages of $2 000 000 as a result of Agency's breach. Agency however contended that they did not owe a duty to Westfield, only to the insured, thus they cannot be liable to Westfield.

The Court of Appeal held that the relationship between Westfield and Agency was defined by the Agreement, which did not impose a duty on Agency to disclose information regarding the insured, nor to act honestly or with due diligence. The Agreement expressly described Agency as an "independent contractor" and not as an employee of Westfield. Thus as a matter of the law, Agency did not owe any duty to Westfield and was entitled to the summary judgment. The Court of Appeals however reversed the summary judgment pertaining to Westfield's fraudulent misrepresentation claim.

5.5.5 Kansas

- *Weinlood v Fisher & Associates Inc.* 1999 Kan.App. 2d 20

As in *Grigsby v Mountain Valley Ins. Agency Inc.*[141] the court held that the insured's failure to read their homeowner's policy was of no legal consequence and rejected the brokers' argument that the insured had a duty to read their policy thus allowing the claim for professional negligence against the broker. It was held that the broker owed a duty to exercise care, skill, and diligence of a reasonable prudent and competent agent, the failure of which amounted to the breach of duties owed to the insured.

[141] *Grigsby v Mountain Valley Ins. Agency Inc. 1990 795 S.W. 2d 372*

5.5.6 Maryland

- *Charles S. Jones et ux v Hyatt Insurance Agency Inc.* 1999 741 A.2d 1099

The action was brought by tort claimants against an insurance agency in contract as third-party beneficiaries of the contract based upon the agency's negligence in failing to procure motor vehicle liability insurance for its client. The Court of Appeals of Maryland held that the tort claimants had no viable cause of action in tort against the insurance agency as the agency did not owe them a duty independent of the contract.

- *Evelyn E. Sadler v The Loomis Company* 2001 139 Md. App. 374, 776 A.2d 25, Md. App. Lexix 118

Sadler was involved in a motor vehicle accident resulting in the other driver, Timothy Prophet, having to amputate his leg. Sadler procured insurance through The Loomis Company and had an automobile policy with a limit of $100 000. When Sadler realised these limits were insufficient for the claim, she transferred the rights of her home at an extremely undervalued amount to her siblings. Prophet learned of this transfer and filed a second suit against Sadler and her siblings alleging fraud. Sadler eventually settled the lawsuits with the automobile policy contributing the maximum amount of $100 000. Sadler then filed a suit against Loomis alleging that as her insurance broker, Loomis owed her a duty to provide her with unsolicited advice regarding the adequate level of liability coverage. The court held that an insurance broker is under no duty to render unsolicited advice concerning liability coverage.

- *Insurance Co. of North America v Miller* 2001 765 A.2d 587

The Insurance Company of North America (INA) contracted with broker J.L. Hickman & Company who employed Miller as an insurance agent. Hickman agreed to act as INA's agent but when Hickman went out of business INA discovered that Hickman and Miller had been retaining premiums instead of forwarding them to the INA. INA then sued Miller personally for negligence. Maryland's highest court upheld the claim stating the as INA's agent Miller owed a

duty to INA. The court thus permitted INA to institute a negligence claim against Miller as he was under a duty as an agent and fiduciary to act in INA's interest.

- *Lawyers Title Insurance Corporation v Rex Title Corporation* 2002 282 F.3d 292

Lawyers Title Insurance Corporation, an insurance provider, instituted an action for negligence against its agent, Rex. The magistrate judge ruled in favour of Rex stating that Maryland law does not allow an insurance company that has entered into an agency agreement with an insurance agent to bring a claim of negligence against the agent. The Court of Appeal however reversed this judgment stating that Maryland does recognize that an insurance agent owes a duty of care to its principal.

5.5.7 Massachusetts

- *Southeastern Insurance Agency Inc. v Lumbermens Mutual Insurance Company* 1995 38 Mass. App 642

It was held that where the insurance broker's negligence in failing to request, in a timely manner, that the insurer provides additional coverage under a liability policy was not the proximate cause of the insurer's loss, then the insurer was not entitled to indemnification from the broker.

- *Riley v Commercial Insurance Agency Inc.* 1999 Mass.App.Div 243

The issue of whether an insurance agent's failure to obtain temporary housing coverage for the insured was a violation of Massachusetts General Laws Chapter 93A was addressed. This law deals with unfair and deceptive acts in commerce and provides a separate cause of action from negligence and breach of contract, allowing for its own standard of liability. The judge held that the agent had in fact violated Chapter 93A by committing acts which fell under the definition of 'unfair and deceptive'.

- *St. Paul Surplus Lines Ins. Co. v Feingold Ins. Agency Inc.* 1998 427 Mass. 372

An application for the insurance of a restaurant failed to mention certain material facts, which if the insurer had known of, would not have provided the insurance. The broker knew that the insurer may not accept the insurance as another insurer had already refused cover and thus put incorrect information on the application form. The court held that the broker was liable to the insurer for negligently or recklessly putting incorrect information on the form as the broker should have reasonably known that the insurer would otherwise not have granted the insurance. Furthermore this misrepresentation constituted a violation the Massachusetts General Laws Chapter 93A.

5.5.8 Montana

- *Gay v Lavina State Bank* 1921 202 P. 753 Mont

In 1921 the Lavina State Bank operated an insurance business writing hail insurance for Hartford Fire Insurance Company. Gay signed a promissory note with the bank to pay for hail insurance. The court held that the claim was one of breach of contract to procure insurance and stated that the bank was a broker as opposed to an agent. The court stated as follows:

> "Every broker is within a sense an agent, but every agent is not a broker. The chief feature which distinguishes a broker from other classes of agents is that he is an intermediary, or middleman, and, in accepting applications for insurance, acts in a certain sense as the agent of both parties to the transaction… as between the insured and his own agent or broker, authorized by him to procure insurance, there is the usual obligation on the part of the latter to carry out the instructions given him and faithfully discharge the trust reposed in him, and he may become liable in damages for breach of duty. If he is instructed to procure specific insurance, and fails to do so, he is liable to his principal for the damage suffered by reason of the want of such insurance. The liability of the agent with respect to the loss is that which would have fallen upon the company had the insurance been effected as contemplated. Negligence on the part of the agent, defeating

> in whole or part the insurance which he is directed to secure, will render him liable to his principal for the resulting loss."

- *Fillinger v Northwestern Agency Inc. of Great Falls* 1997 Mont. 938 P.2d 1347

The insured operated a 'guide and outfitting' business in Montana providing hunting and floating trips for customers. The broker knew of the nature of the insured's business but failed to procure adequate coverage. A customer was injured on one of the trips but coverage was denied. The insured then sued the broker for negligence in procuring appropriate insurance coverage. A jury ruled in favour of the insured and the broker appealed. The court held that the insured had no duty to read the policy to determine what type of insurance the broker had procured.

- *Marie Deonier & Associates v Paul Revere Life Ins. Co.* 2000 Mont. 9 P.3d 622, 2004 Mont. 101 P.3d 742 - *("Deonier I and II")*

Two cases, known as Deonier I and II, at the Supreme Court of Montana have recently drawn attention to insurance agents selling disability insurance. The litigation lasted almost 11 years, beginning in 1993 when the claim was first filed and ending in 2004 when the Supreme Court handed down its ruling. Here, Marie Deonier & Associates were a general lines insurance agency who obtained a judgment of $1.2 million against Paul Revere for the breach of fiduciary duties. The Deonier cases established that an insurance company has a duty to disclose to its agents any pecuniary risks that may be faced when selling policies. The court held that an independent insurance broker who is authorized to procure insurance policies is an agent of the insurer and as such owes duties to the insurer and stated that:

> "a soliciting agent of an insurance company is the agent of the insurer and not the insured for the purpose of soliciting and procuring the insurance and preparing the application."

5.5.9 New Jersey

- *Rider v Lynch* 1964 42 N.J. 465

The court held that a policyholder's failure to read the policy did not constitute contributory negligence in an action involving the broker's failure to procure adequate insurance coverage. It was held that it was reasonable for the policyholder to assume that the broker had performed his fiduciary duties, and further that these duties did not diminish due to the policyholder's failure to detect the breach of such duty. Justice Francis stated that:

> "One who holds himself out to the public as an insurance broker is required to have the degree of skill and knowledge requisite to the calling. When engaged by a member of the public to obtain insurance, the law holds him to the exercise of good faith and reasonable skill, care and diligence in the execution of the commission… If he neglects to procure the insurance or if the policy is void or materially deficient or does not provide the coverage he undertook to supply… he becomes liable to his principal for the loss sustained thereby."

- *Sobotor v Prudential Prop. & Cas. Ins. Co.* 1984 N.J. Super. 491 A.2d 737

The appellate court in New Jersey confirmed the trial judges' conclusion that an insurance agent owes a duty to advise his client of the availability of higher monetary limits for the coverage requested. This duty however depends on whether the agent has a special expertise in insurance as well as the length of the relationship between the insured and the agent. The court noted that:

> "[the] fiduciary nature of such a relationship should not depend on the length of the relationship. Because of the increasing complexity of the insurance industry and the specialized knowledge required to understand all of its intricacies, the relationship between an insurance agent and a client is often a fiduciary one. Agents should be required to use their expertise with every client, not only those with whom they have a long-term relationship."

- *Aden v Fortsh* 2001 169 N.J. 64, 776 A.2d 792

A broker sold its client a 'homeowner's policy' for a condominium unit. The condominium was subsequently destroyed by a fire and it was only then that the client discovered that the policy provided only $1000 in coverage. The client sued the broker for failing to procure adequate insurance coverage. A jury ruled in favour of the client but the Appellate division reversed, holding that the trial court had failed to inform the jury that the client had not read the policy. The Supreme Court reversed and reinstated the verdict in favour of the client. The court expressly noted that if the conduct of the insured was the sole and proximate cause of the alleged tort and it was not the fault of the professional then the professional may not be held liable. Moreover, the court stated that a New Jersey insured is entitled to rely upon the broker to perform their fiduciary duties when they are hired to procure insurance and further that the brokers duty does not cease if the policyholder fails to notice that the brokers breach by not reading the policy. The court stated that:

> "In view of New Jersey's tradition of holding insurance professionals and other fiduciaries to higher standards, we conclude that [the insured's] failure to read the insurance policy cannot be asserted as comparative negligence in an action against the broker for negligent failure to procure insurance."

- *President v Jenkins* 2004 WL 1737725

The plaintiff's brought a suit against an obstetrician, Dr. Jenkins, alleging negligence. Dr. Jenkins cross-claimed against his insurance broker when his professional liability insurers repudiated cover, claiming a gap in coverage on his medical malpractice insurance policy. He alleged that the broker had failed to advise him of the availability of gap coverage to fill the period between the end of his previous cover and the beginning of his new policy. The trial court however dismissed all claims against the broker. The Supreme Court concurred by stating the long-standing New Jersey standards of duties owed by brokers.

5.5.10 New York State

- *Israelson v Williams* 1915 166 A.D. 25

This case was one of the earliest cases dealing with broker liability. The insured hired a broker, Williams, to arrange fire insurance and advised him other insurance was already in place. The broker however obtained coverage that contained a provision which made the policy void if there was other insurance, unless expressly permitted. A fire destroyed the property and the insurer denied cover on the grounds of the provision requiring the permission of other insurance. The insured then sued the broker alleging negligence in the performance of duties. The broker argues that the insured, having failed to read the policy, exonerated the broker from the negligence claim. The court held that the insured:

> "had the right to rely upon a presumed obedience to his instructions on part of his skilled [broker] and [the insured] was not negligent in taking steps to investigate the matter."

5.5.11 Oregon

- *Franklin v Western Pacific Ins. Co.* 1966 414 P.2d 343

The broker failed to mention to the insured's that the fire insurance policy which was procured on their behalf was conditioned on the insured's maintaining their existing policy. The court rejected the brokers' argument that the insured's should have read the policy and relied on the decision in the New York State case of *Israelson* in reasoning that the insured's could depend on the broker to provide them with coverage suitable to their needs and instructions.

5.5.12 Tennessee

- *Ebbtide Corporation v The Travelers Insurance Company et al.* 2001 Tenn. App. Lexis 5582001

The broker, Willis Corroon, failed to forward the terms of the reinstatement of the insured's, Ebbtide's, workers compensation policy to the insured but did however fax the reinstatement to the insurer. The insured was left without coverage for several months during which time a worker's compensation claim was filed and paid. The trial court established that the Tennessee Code of Annotated section 56-6-147 did not apply to Willis Corroon as an insurance broker and the Willis Corroon was the agent of the insured. Willis Corroon was found to be negligent for the forwarding the policy to the insured and was held liable for all damages incurred by the insured as a result of being uninsured.

The Court of Appeals affirmed the trial court's decision that the broker was liable to its principal for the damages suffered by the reason of the want of insurance. Willis Corroon was, under the laws of the State of Tennessee, an agent of Ebbtide and as such had breached its duty in failing to forward the reinstatement requirements to Ebbtide. Ebbtide breached its contract with Travelers as a result of Willis Corroons breach of duty. The breach of the contract between Ebbtide and Travelers was further proximately caused by Willis Corroon's negligence, and as a result, Willis Corroon was held liable for all the ensuing damages.

5.5.13 Texas

- *Grigsby v Mountain Valley Ins. Agency Inc.* 1990 795 S.W. 2d 372

The insured, who owned two warehouses, procured insurance for these warehouses through a broker. The broker however arranged insurance for only one of the warehouses. A fire destroyed one of the warehouses, the one for which the broker had not provided insurance. The insured sued the broker for professional negligence in failing to procure adequate coverage. The

broker however argued that the insured was contributorily negligent as he had not read the policy. The Kentucky Supreme Court rejected the brokers' defense and stated that:

> "Due to the highly technical nature of fire insurance policies, an insured may not he held contributorily negligent for the failure to read and understand his or her coverage… We hold that a claim based upon the negligence of the agent to properly provide coverage is also not affected by the insured's failure to read and understand the policy."

- *May v United Services Association of America* 1992 844 S.W.2d 666

The plaintiff's sued their insurance agent for negligence and misrepresentation. The jury found for the Mays on the negligence claim but not on the misrepresentation claim. The Court of Appeals however reversed the negligence finding. The Supreme Court affirmed the decision of the appeals court stating that:

> "[t]he Mays claim that [the agent] was negligent because he should have known of the risk posed to them by the potential shifting of the underwritings,… they offer no evidence as to why this risk was unjustified for them in particular, or why [the agent] should have prevented them from assuming it."

- *Insurance Network of Texas v Kloesel* 2008 266 S.W.3d 456

Harvey and Diana Kloesel individually sued the Insurance Network of Texas (INT), their insurance agent, for breach of contract, negligence, and violations of the Texas Insurance code and the Texas Deceptive Trade Practices Act. At the trial court the Kloesel's obtained a favourable jury verdict concluding that: INT committed negligence which was the proximate cause of the Kloesel's damage and INT knowingly made misrepresentations relating to the Kloesel's insurance policy. On appeal, the court addressed the main issue of whether an agent can be held liable for negligence in procuring a policy; the court found that an agent could be held liable.

5.5.14 Summary

The following table provides an illustration of the liabilities and duties across various states.

State	Year	Case	Breach in contract	Breach in tort	Breach of statute	Failure to obtain adequate insurance	Duty to exercise reasonable skill, care and diligence owed	Failure to carry out instructions of insured promptly and diligently	Failure to procure insurance	Negligence	Special undertaking	Duty to investigate/inquire	Duty to advise
Alaska	1980	Clary Insurance Agency v. Doyle 620 P.2d 194				x							
Arizona	1967	Oney v. Barnes 5 Ariz. App. 460, 428 P.2d 124	x			x							
	1984	Darner Motor Sales v. Universal Underwriters 140 Ariz. 383, 682 P.2d 388					x						
California	1954	Valdez v. Raylor 129 Cal. App. 2d 810, 822-823, 278 P.2d 91				x							
	1970	Mid-Century v. Hutsel 10 Cal. App. 3d 1065, 1068, 1069, 89 Cal. Rptr. 412				x							
	2003	Wolfe Air Aviation Ltd. V. Bartling 2003 WL 21290926 (Cal. App. 2)									x		
Colorado	1952	Mitton v. Granite State 196 F.2d 988, 989						x					
	1987	Bayly, Martin & Fay v. Pete's Satire 739 P.2d 239, 243							x				
	2003	Admiral Insurance Co. v. Cresent Hill Apartments 328 F.3d 1310									x		
Connecticut	1934	Ursini v. Goldman 118 Conn. 554, 173 A. 789				x	x						
	1986	Dimeo V. Burns, Brooks & McNeil Inc. 6 Conn App. 241, 504 A.2d 557, 199 Conn. 805, 508 A.2d 31				x	x						
	1990	Rametta v. Stella 214 Conn. 484, 485	x	x					x				
	1997	Hallas v. Boehmke & Dobosz 239 Conn. 658, 686 A.2d 491					x						
	2001	Sadler v. Loomis Co. 776 A.2d 25											x

State	Year	Case	Breach in contract	Breach in tort	Breach of statute	Failure to obtain adequate insurance	Duty to exercise reasonable skill, care and diligence owed	Failure to carry out instructions of insured promptly and diligently	Failure to procure insurance	Negligence	Special undertaking	Duty to investigate/inquire	Duty to advise
Connecticut	2002	Cooper v. Bershire Life Ins. Co. 810 A.d 1045								x			
	2003	Al's Café Inc. v. Saunders Insurance Agency 820 A.2d 745										x	
	2003	President v. Jenkins 814 A.2d 1173											x
Florida	1977	Neida's Boutique Inc. v. Gabor & Co. 348 So. 2d 1196							x				
	1988	Warehouse Foods Inc. v. Corp. Risk. Mgt. 530 So. 2d 422							x				
Georgia	1990	Bryne v. Reardon 196 Ga. App. 735, 397 S.E.2d 22					x	x					
	2002	Pitts v. Jackson National Life Ins. Co. 574 S.E.2d 502											x
Indiana	1986	Steward v. City of Mt. Vernon 497 N.E.2d 939, 942							x				
	2002	The Island House Inn. Inc. v. State Auto Insurance Companies 782 N.E.2d 156											x
	2003	De Hayes Group v. Pretzels Inc. 786 N.E.2d 779											x
	2007	Dreibelbiss Title Co. Inc. v. MorEquity Inc. 561 N.E.2d 1218 1222							x				
	2009	Brennan v. Hall 904 N.E.2d 383, 386					x		x				
Iowa	1976	Smith v. State Farm 248 N.W.2d 903, 905					x						
	1994	Humiston v. Rowley 512 N.W.2d 573, 574-75					x						
	2002	Poluk V. J.N. Manson Agency Inc. 653 N.W.2d 905										x	

State	Year	Case	Breach in contract	Breach in tort	Breach of statute	Failure to obtain adequate insurance	Duty to exercise reasonable skill, care and diligence owed	Failure to carry out instructions of insured promptly and diligently	Failure to procure insurance	Negligence	Special undertaking	Duty to investigate/inquire	Duty to advise
Kansas	1972	Keith v. Schiefen-Stockton Ins. 209 Kan. 537, 499 P.2d 265							x				
	1977	Blair v. Fidelity Life Association 1 Kan. App. 2d 382, 567 P.2d							x				
	1981	Marshel Investments Inc. v. Cohen 6 Kan. App. 2d 634 P.2d 133	x	x									
Mississippi	1991	Bass v. California Life Ins. Co. 581 So. 2d 1987		x						x			
	1994	Taylor Mach. Works v. Great Amer. Surplus Lines Ins. 635 So. 2d 1375							x				
	2002	Graves v. State Farm Mutual Auto Ins. Co. 821 So.2d 769										x	
New Jersey	2002	Rapp v. Awany 205 F.Supp.2d 279										x	
New York State	1999	Stephens v. Hickey-Finn & Co. Inc. 261 A.D.2d300 N.Y.S.2d 411									x		
	2001	State Insurance Fund v. Richard Anderson Trucking Inc. 722 N.Y.S.2d 816											x
	2001	Storybook Farms. V. Ruchman Associates Inc. 726 N.Y.S.2d 867											x
	2003	Tappan Wire & Cable Inc. v. County of Rockland N.Y. Slip Op. 14530 2003 WL 21221703											x
	2003	Coventry Coating Corp. v. Verlan Fire Ins. Co. 756 N.Y.S.2d 185											x

State	Year	Case	Breach in contract	Breach in tort	Breach of statute	Failure to obtain adequate insurance	Duty to exercise reasonable skill, care and diligence owed	Failure to carry out instructions of insured promptly and diligently	Failure to procure insurance	Negligence	Special undertaking	Duty to investigate/inquire	Duty to advise
New York State	2003	Ficarra v. Security Mutual Ins. Co. 757 N.Y.S.2d 59								x			
South Dakota	1975	Moore v. Kluthe & Lane Ins. 89 S.D. 419, 234 N.W.2d 260					x						
	1978	Fleming v. Torrey 273 N.W.2d 169							x				
Texas	1929	Stevens v. Wafer 14 S.W.2d 295, 296	x										
	2002	Nast. v. State Farm Fire and Cas. Co. 82 S.W.3d 114											x
	2003	Jones v. Kennedy 108 S.W.3d 203									x		
Wisconsin	1969	Hause v. Schesek 42 Wis. 2d 628, 167 N.W.2d 421							x				
	1994	Appleton Chinese Food Servv. Inc. v. Murken Ins. Inc. 185 Wis. 2d 791, 519 N.W.2d 674						x	x				

Table 1: Illustration of liabilities and duties of insurance intermediaries across various States

5.6 Canadian case law

- *Fine Flowers Limited v General Accident Assurance Company of Canada* 1977 81 DLR 139

The broker was instructed to obtain full coverage for a horticultural business. When a water pump failed the plants were destroyed and it was alleged that the loss was not covered by the policy. The Ontario Court of Appeal held that the broker breached his duty of care as he was instructed to obtain cover for all foreseeable normal insurable risks and that the risk of freezing was obvious.

5.7 Hong Kong case law

- *Pacific Dunlop (Asia) Ltd. & Grosby (Chine) Ltd. v Inchape Insurance Brokers (HK) Ltd.* 2001 HKEC 806

Dunlop Asia and its subsidiary, Grosby China, insured certain factory materials under a policy issued on behalf of the People's Insurance Company of China (PICC) with the brokers Inchape. The policy, dated 6 November 1992, succeeded a September policy. On 25th of November 1992 a fire at the factory caused considerable damaged to the insured property. PICC denied the increase of values stated of the claim under the November policy. Dunlop Asia accepted a lesser settlement and the insurers then claimed this amount from Inchape under subrogation. Furthermore, at the time in question it was illegal (under Section 6 of the Insurance Companies Ordinance) for Inchape to issue a PICC policy in Hong Kong.

The judge however held that Inchape had full authority to issue policies on behalf of PICC and found that:

> "nothing in this argument… it and in so far as the Ordinance has any application to the present situation [that is an insurance policy covering non-Hong Kong risks issued by a non-Hong Kong insurance company], the point goes nowhere because section 6 of the

Ordinance gives the plaintiffs as policy holder the option, as against the insurer, to treat the policy as valid or void."

5.8 Conclusion

The liabilities of insurance intermediaries appear to be fairly consistent across most countries and states. However it must be noted that the ultimate decision of the liability of the insurance intermediary lies at the hands of the court making it virtually impossible to generalise any specific conclusions.

Certain duties of the insurance intermediary do nonetheless seem to be reiterated by most courts. Most notably the insurance intermediary has a duty to exercise reasonable skill, care and diligence.

It has furthermore been established that an insurance intermediary may be held liable concurrently in contract and tort, as well as for the breach of a statute and a breach of fiduciary duties. The insurance intermediary may also be held liable for the failure to procure insurance, the failure to procure the adequate insurance, the failure to carry out the insured's instructions promptly and diligently, and for negligence on the part of the intermediary.

Ziomek and McCahill (1999) note that in the United States, legal liabilities have been imposed upon insurance intermediaries in the following situations (this list however is not exhaustive):

a) Failure to obtain coverage for the insured as agreed upon.
b) Failure to promptly advise the insured of the denial of coverage.
c) Where the intermediary is relied upon as a specialist.
d) Where the intermediary has made oral assurances to place the insurance but has failed to do so.
e) Failure to place insurance on the best possible terms.
f) Duty to place insurance with a solvent insurer.

6. INSURANCE PRICING

The implications of the liabilities faced by insurance intermediaries' means that insurers are faced with increasingly more claims by insurance intermediaries under professional indemnity policies. This raises the question of how the insurer should appropriately price for these risks. Hickman and Miller (1970) note that the principles of pricing date back to 1762 with the establishment of The Equitable of London, a life insurance company, using principles developed by James Dodson, a British mathematician and actuary. These principles were developed by Dodson in 1756 when he calculated the first table of annual premiums, building upon the mortality tables developed by Edmund Halley in 1693, which the Society of Equitable Assurances would eventually use to base their premium calculations on.

Insurance is an operation whereby the insurer promises to indemnify the insured in exchange for a payment, called a premium; by attaching a premium to each risk, an insurer has implicitly ordered the risk (Stettler, Eugster, and Kuhn; 2005; Wang; 1995: 43).

Harrington and Niehaus (2003: 134) note that if insurers are to sell coverage, they must receive premiums which both funds their expected claim costs and provides them with a profit that compensates them for the cost of obtaining the capital necessary to support the sale of coverage; this is known as the fair premium. In order to price insurance policies reasonably, insurers must predict accurately the expected loss, often referred to as the 'pure premium', for policyholders (Hsiao, Kim, Taylor; 1990: 5-6).

Gogol (1993: 119) suggests that the expected profitability of a risk depends on the relation between the risk's expected losses and its experience-modified premium and further notes that if an insurer charges too much for a risk, it is likely to lose that business, and if it charges too little, it is likely to lose money. Moreover Wang (1995) notes that a higher premium will be charged for risks that are more uncertain; this additional premium is called the risk load (Meyers; 1991).

Furthermore competition will prevent an insurer from charging premiums that are much greater than their expected claim costs. As noted by Harrington and Niehaus (2003), in a competitive market, differences in expected claim costs will produce differences in premiums so long as:

(i) insurers want to make money;
(ii) insured's seek policies with low premiums for a given amount of coverage;
(iii) insurers can predict the differences in expected claim costs at a low cost.

"A common problem in all areas of insurance is the proper pricing of a policy based on what is known about the individual being insured… It is theoretically possible for a shrewd underwriter to benefit at least temporarily by identifying segments of the market that are currently being overcharged and offering coverage at lower rates or by avoiding segments that are being undercharged" (Hsiao, Kim, Taylor; 1990: 20).

6.1 Increased limits factors

Lange (1969) notes that in ratemaking, a loss ratio or pure premium approach is usually applied, however neither of these works well with increased limits. Palmer (2007) notes that the current technique used to determine the appropriate charges for varying limits of liability is to calculate a series of factors, known as increased limits factors.

Ludwig (1991: 399) notes that the Salzmann Tables, developed by Salzmann (1963), represent an 'exposure rating' technique to price excess of loss reinsurance: "Exposure rating does not rely on the ceding company's actual loss history as a basis for developing a reinsurance rate, but rather on their distribution of direct premium by policy limit. For each policy limit written by the ceding company, an estimate is made as to the proportion of losses that fall within the reinsurance layer being priced. In casualty reinsurance, one standard means of estimating these proportions is through the use of increased limits factors, while in property reinsurance, Salzmann Tables serve an equivalent function".

Liability policies are generally sold with a range of policy limits. The limit of liability clause of the professional indemnity policy, as discussed in Section 3.2.3, limits the insurers' exposure to

the insured risk by setting a maximum amount for which the insurer may be liable to pay; this limit may either be an aggregate limit or a limit per claim. "The large risk associated with high limits coverage can be significantly reduced by 'vertical' layering. This type of layering can be effected by two methods. The first is by insuring through two or more underwriters, one underwriter providing 'first-dollar' coverage and the others excess of loss coverage. The second is through non-proportional reinsurance" (Miccolis; 1977: 45). Any number of layers in excess of loss coverage may be available depending on the degree of risk an insurer wishes to retain. The following figure illustrates the principle of layering:

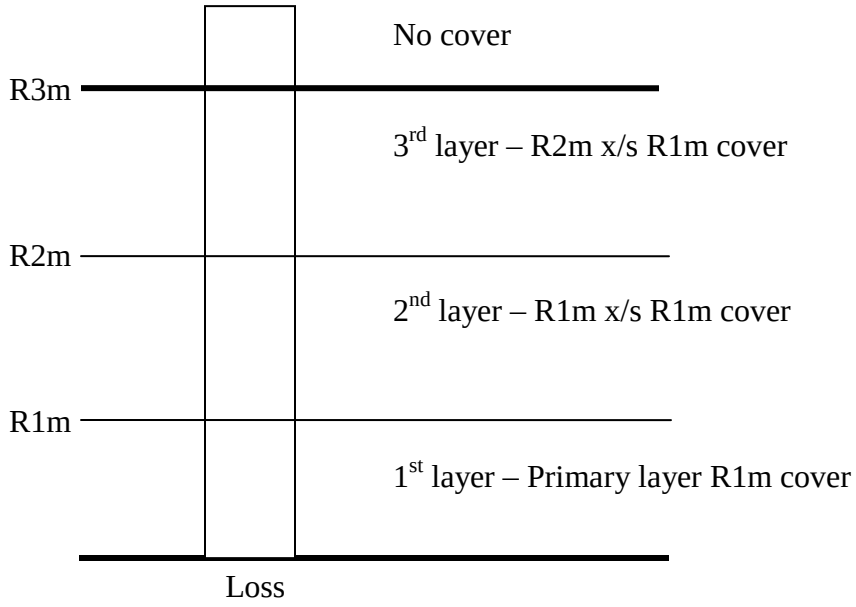

Figure 1: The principle of layering

Ferguson (1972) notes that the first layer will experience the highest claim frequency and thus may be experience rated while all successive layers will have a low claim frequency.

Meyers (1991) notes that as the policy limits increases, so does the premium. Should the insured wish to increase his coverage beyond the current limit of liability, the insurer must determine a charge (that is additional premium) for this extra coverage over and above the primary layer; this is done through the use of increased limits factors. Thorpe (2004) notes that the increased limits

factor should increase at a decreasing rate as the limit of indemnity increases and that expected costs per unit of coverage should not increase in successively higher layers.

Palmer (2007) notes that an important reason for the usage of increased limits factors is credibility; more data will mean more reliable estimates. However as the limit of indemnity increases, data loses its credibility (Barclay and Marquardt; 1990); Miccolis (1977) further notes that as at 1977 there was little experience on losses in liability insurance in excess of $500 000 per occurrence and moreover that the probability that a loss would exceed this amount is quite small.

In the United States, to solve this problem, Palmer (2007) and Barclay and Marquardt (1990) note that the analysis is split in two: first the larger volume of data available for relatively smaller limits are calculated for full classes or individual states and then increased limits factors are calculated using a broader combination of experience, such as countrywide data. However, data should not be merged as severity differs from limit to limit (Klugman; 1990).

Having the correct increased limits factor means that insurers can accurately price any increases in the limit of liability; this will provide insurers with a competitive advantage as those without this knowledge will either over- or under-charge for coverage. Where the increased limits factor is lower than the statistical average, the insurer who has knowledge of the correct increased limits factor stands to make a profit by charging a premium lower than those charged by other insurers. Therefore insurers may accurately determine which businesses will be most profitable for them.

Bartylak (2008) notes that within the South African insurance industry, the South African professional indemnity market charges between 30-40% of the primary layers premium to double the limit of liability as a ‘rule of thumb’ as the correct price that should be charged is not known. Thus if the statistical increased limits factor for R1m in excess of R1m cover was 25%, an insurer could stand to profit as the market would be overcharging.

6.2 Rate on line

The Reinsurance Association of America (2003: 31) defines 'payback' as a method of rating under which the underwriter sets the price based upon his view of how frequently the loss event might occur over a period of time; where a loss is estimated to occur once in five years the price is set to be equal to the limit divided by five. Schmidt (1987) notes that the rate on line is effectively the inverse of the payback period, thus a five year payback is equivalent to 20% rate on line.

Sundt (1991) notes that the rate on line is calculated by dividing the premium by the limit and is usually stated as a percentage. In the market, a minimum rate on line is generally justified by underwriters as a charge for using their surplus or capital (Kreps; 1999). Thus the rate on line is the minimum premium the insurer will charge per limit of coverage. Cholnoky, Heimermann and Cheung (2004) suggest that the rate on line should be much more uniform above the primary layer with smaller deviations in price between the layers.

Hartwig (2004) notes that with worldwide reinsurance prices rising, limits are falling resulting in significantly higher rates on line.

The rate on line therefore provides a qualification to the increased limits factors. Increased limits factors which are not greater than the rate on line will not be used as insurers must earn a minimum premium amount that covers them for their risk exposure and use of capital. In this situation insurers will use their discretion and previous experience when calculating the appropriate premium charge.

6.3 Deductible

The deductible is that amount of the loss which the insured must bear; the first Rx of each and every claim. Braun and Muermann (2004: 737) note that for insurance policies that are structured with a deductible, indemnity is a payoff for the loss above a certain threshold. The

limit of liability is this threshold amount and is thus in excess of the deductible. Core (1997) notes that insurers will generally charge a higher deductible when litigation risk is higher.

7. EMPIRICAL ANALYSIS

The empirical analysis section of this dissertationt seeks to determine the increased limits factor that should be applied when pricing professional indemnity policies for insurance intermediaries, as well as the applicable deductible credits and rate on line percentages. An analysis of the types of claims against insurance intermediaries will also be conducted.

7.1 Data

The data used was obtained from two confidential source; it is representative of the South African insurance intermediaries professional indemnity market, as confirmed by North (personal communication; 2008) and Liebenberg (personal communication; 2008).

The data was sorted and only incurred amounts with positive values were included in the analysis, with any duplicates being deleted and negative values being allocated to their respective claims. Where a deductible figure was not provided for in the data, a reasonable estimate based upon a confidential consultants experience was used.

7.1.1 Inflation

In order to calculate the increased limits factors, the amount of the claim payments must be known at the values they represent today. The values of claim payments in the data are recorded at the value they represented in the year they were recorded; thus all payments must be inflated.

The data was inflated at an undisclosed appropriate inflation factor (so as to preserve the confidentiality of the data) for the years 1986-2008 with the base year being 2008. All the data

used in the calculation of the increased limits factors thus represents the claim payments at their inflated value at December 2008 with any claims during or after 2008 not being inflated.

The following formula was used in the calculation of the inflated claim amount:

Inflated value = (Gross claim amount paid x Inflation rate) + Gross provision amount + Deductible

where: 'Inflated value' is the value of the claim today, 'Gross claim amount paid' is the amount that has already been paid for the claim, 'Gross provision amount' is the provision provided by the insurer for the future payment of the claim, and 'Inflation rate' is the appropriate inflation rate for each respective year.

As all claims are reflected net of the deductible, the deductible is not inflated as it is accounted for when the claim is paid.

Furthermore, the reserve amount is not inflated as it is revised yearly by the underwriter or their claims staff.

The following basic example illustrates the calculation of the inflated (as at 2008) value of the claim:

Consider a claim in 2003 with the Gross claim amount of R5 000, the Gross reserve amount of R0, a Deductible of R2 500, and an appropriate inflation rate of 1.2%. The inflated value will be calculated as follows:

Inflated value = (R5 000 x 1.2%) + R0 + R2 500
= R8 500

Thus the value of the claim today will be R8 500.

Furthermore none of the inflated claim values exceed the policies' limits of indemnity.

7.1.2 Methodology – Increased limits factors

The claim amounts, converted to their current value, are used to calculate the appropriate increased limits factor.

The calculation of the increased limits factor answers the following question: If an insured wishes to increase his cover, by how much should the insurer increase the premium?

The following simplistic example illustrates how the increased limits factor is calculated given a primary layer of R500 000 and an excess layer of R1m to provide R1.5m coverage; that is, R1m in excess of the deductible.

Consider the following table:

Current value of claim in excess of deductible (R'000)	**1st R500 000 of claims (R'000)**	**R1m xs R500 000 (R'000)**
250	250	0
370	370	0
480	480	0
530	500	30
990	500	490
1 600	500	1 000
Total	2 600	1 520

Table 2: Calculation of the increased limits factors example

The 'Current value of claim' represents the inflated value of each claim payment, the '1st R500 000 of claims' represents the first R500 000 (in excess of the deductible) that the insurer will pay (any value exceeding R500 000 is not covered and will not be paid), and 'R1m xs R500 000' represents the excess layer of R1m where the insurer will pay the difference between the current value of the claim and the first layer of coverage (that is R500 000) up to R1m.

Thus any claim up to and including R500 000 will be paid by the primary policy and any claims above R500 000 will be paid by the excess policy up to the value of R1m. Any amount of a claim exceeding R1.5m will not be covered.

The increased limits factor is calculated as follows:

[Total of 'R1m xs R500 000' / Total of '1st R500 000 of claims] x 100

= [R1 520 000/R2 600 000] x 100

= 58.46%

Therefore to provide the extra R1m of cover, the insurer should charge 58.46% of the primary policy's original premium. Thus assumes that the primary policy is adequately priced.

7.1.3 Methodology – Deductible credits

As with the calculation of the increased limits factors, the inflated claim amounts were used to calculate the appropriate deductible credits. However, in the calculation of the deductible credits the individual claims data was restricted to a maximum of R1m. As noted by Ferguson (1972) the primary layer experiences the highest frequency of claims thus the data is limited to R1m as the deductible has the greatest impact up to this amount; this has been confirmed by Liebenberg (personal communication; 2009)

The following simplistic example illustrates how the deductible credits were calculated.

Inflated value of claim (R'000)	**Claim's values (R'000) Max R1m**	**Claim value net of R10 000 deductible (R'000)**
5	5	0
12	12	2
170	170	160
550	550	540
640	640	630
880	880	870
1 100	1 000	1 000
1 300	1 000	1 000
2 500	1 000	1 000
Total	5 257	5 202

Table 3: Calculation of deductible credits example

The 'Claim value net R10 000 deductible' is the amount of the claim the insurer will pay after the deductible of R10 000 (the insured bears the first R10 000 of the claim).

The deductible credit is calculated as follows:

[Total of 'Max R1m for all claims' – Total of 'Claim value net R10 000 deductible] / Total of 'Max R1m for all claims' x 100

= [5 257 000 – 5 202 000]/5 257 000 x 100

= 1.05%

Therefore if the insured has a deductible of R10 000, the insurer may reduce the premium by 1.05%. Higher deductibles should receive higher deductible credits and thus result in less premium to be paid.

7.1.4 Methodology – Rate on line

The gross incurred amounts (which exclude the deductible) were used in the calculation of the rate on line percentages. The inflated claim value is not used in this calculation as the limits of indemnities are not inflated amounts and as such must be compared with the non-inflated claim values, which are reflected by the gross incurred amount. The rate on line is the ratio of premiums to limit (Schmidt; 1987) and is calculated using the following formula:

$$\text{Rate on line} = \frac{\text{Sum of all claims per a limit of indemnity}}{\text{Sum of limit of indemnity for all claims}} \times 100$$

The following provides an example of the calculation of the rate on line percentage for a limit of indemnity of R500 000 with 6 claims.

Limit of indemnity	**Gross incurred amount**
R500 000	R10 000
R500 000	R70 000
R500 000	R250 000
R500 000	R330 000
R500 000	R490 000
R500 000	R620 000
R3 000 000	R1 770 000

Table 4: Calculation of rate on line example

$$\text{Rate on line} = \frac{\text{Sum of all claims per a limit of indemnity}}{\text{Sum of limit of indemnity for all claims}} \times 100$$

$$= (\text{R1 770 000}/\text{R3 000 000}) \times 100$$

$$= 59\%$$

Thus the minimum premium an insurer would charge for a limit of indemnity of R500 000 would be 59%. A high rate on line percentage is expected for a low limit of indemnity as the lower layers of coverage will experience the highest claim frequency.

7.2 Results – Increased limits factors

The following primary and excess of loss layers were used in the calculation of the increased limits factor:

- R500 000 excess R500 000 i.e. R1m total cover
- R1m excess R1m i.e. R2m total cover
- R1.5m excess R1m i.e. R2.5m total cover
- R2.5m excess R2.5m i.e. R5m total cover
- R2.5m excess R5m i.e. R7.5m total cover
- R5m excess R5m i.e. R10m total cover
- R10m excess R5m i.e. R15m total cover
- R10m excess R10m i.e. R20m total cover.

Table 3 shows the increased limits factor that should be applied to the primary policy's premium when determining the additional premium to be charged to insurance intermediaries for the respective additional cover.

Increased limits factors							
R500 000 xs R500 000	R1m xs R1m	R1.5m xs R1m	R2.5m xs R2.5m	R2.5m xs R5m	R5m xs R5m	R10m xs R5m	R10m xs R10m
24.0%	24.1%	29.9%	16.5%	4.6%	5.4%	1.6%	3.3%

Table 5: Increased limits factors to be applied to primary policy

The above table indicates that, for example, should the insured wish to double coverage from R500 000 to R1m, that is R500 000 xs R500 000 (to purchase a layer of R500 000), then the insurer should charge an additional 24.0% of the original policy's premium.

As previously stated, in the South African professional indemnity market insurers charge about 30-40% to double a limit of liability. The results of Table 4 however indicate that insurers should be charging approximately 24% to double the limit of liability from R500 000 to R1m. Thus the market is in fact overcharging and an insurer could potentially gain a profit by charging less than other insurers.

7.3 Results – Deductible credits

The following deductibles were used in the calculation of the deductible credits: R5 000, R10 000, R25 000, R50 000, R100 000, R250 000.

Table 4 shows the deductible credits that should be applied to reduce the premium charge for insurance intermediaries.

Deductible credits for limits of indemnity ≤ R1m					
R5 000	R10 000	R25 000	R50 000	R100 000	R250 000
3.0%	5.8%	13.3%	22.8%	35.6%	54.6%

Table 6: Deductible credits to be applied to reduce premium

Table 4 indicates that lower deductible values will result in lower deductible credits. Therefore the higher the deductible, the higher the deductible credit, the less premium that should be paid. For example, with a deductible of R5 000, the insured should receive a deductible credit of 3.0%, however with a deductible of R250 000 the insured should receive a deductible credit of 54.6%.

7.4 Results – Rate on line

The following limits of indemnity were used in the rate on line calculations: R100 000, R150 000, R200 000, R250 000, R300 000, R350 000, R400 000, R450 000, R500 000, R750 000, R1 000 000, R1 500 000, R2 000 000, R2 500 000, R3 000 000, R4 000 000, R5 000 000, R6 000

000, R10 000 000, R15 000 000, R20 000 000, R25 000 000, R30 000 000, R50 000 000, R75 000 000, R100 000 000.

The number of claims per limit of indemnity is also displayed. It should be noted that limits of indemnity with higher numbers of claims will reflect more accurate rate on line percentages.

No. of claims per limit of indemnity	**Limit of indemnity R'000**	**Rate on line**
21	100	27.9%
3	150	8.9%
22	200	9.1%
58	250	13.8%
9	300	11.6%
2	350	7.3%
5	400	12.2%
3	450	13.7%
128	500	5.7%
2	700	11.5%
21	750	4.4%
234	1000	7.0%
87	1500	6.5%
95	2000	4.0%
41	2500	7.5%
26	3000	3.8%
8	4000	11.9%
182	5000	3.2%
4	6000	0.9%
83	10000	1.6%
9	15000	0.7%
15	20000	3.6%

No. of claims per limit of indemnity	Limit of indemnity R'000	Rate on line
3	25000	0.6%
7	30000	0.6%
8	50000	0.2%
15	75000	0.1%
3	100000	3.3%

Table 7: Rate on line percentages per limit of indemnity

From Table 6 it is evident that lower limits of indemnity result in higher rate on line percentages, indicating that lower limits experience higher claim frequencies, as expected.

As previously discussed, increased limits factors which are not greater than the rate on line will not be used as insurers must earn a minimum premium amount that covers them for their risk exposure and use of capital. The following table provides a comparison of the increased limits factors calculated for insurance intermediaries and the corresponding rate on line percentages for each limit of indemnity:

Limit of indemnity (Rm)	Increased limits factor	Rate on line
1	24%	7%
2	24.1%	4%
2.5	29.9%	7.5%
5	16.5%	3.2%
10	5.4%	1.6%
20	3.3%	3.6%

Table 8: Comparison of increased limits factors and rates on line

From Table 8 it is evident that all the increased limits factors are greater than the corresponding rate on line percentages and should thus be used when calculating premiums.

7.5 Claims per year

The numbers of claims per year were summed and are graphed in the figure below:

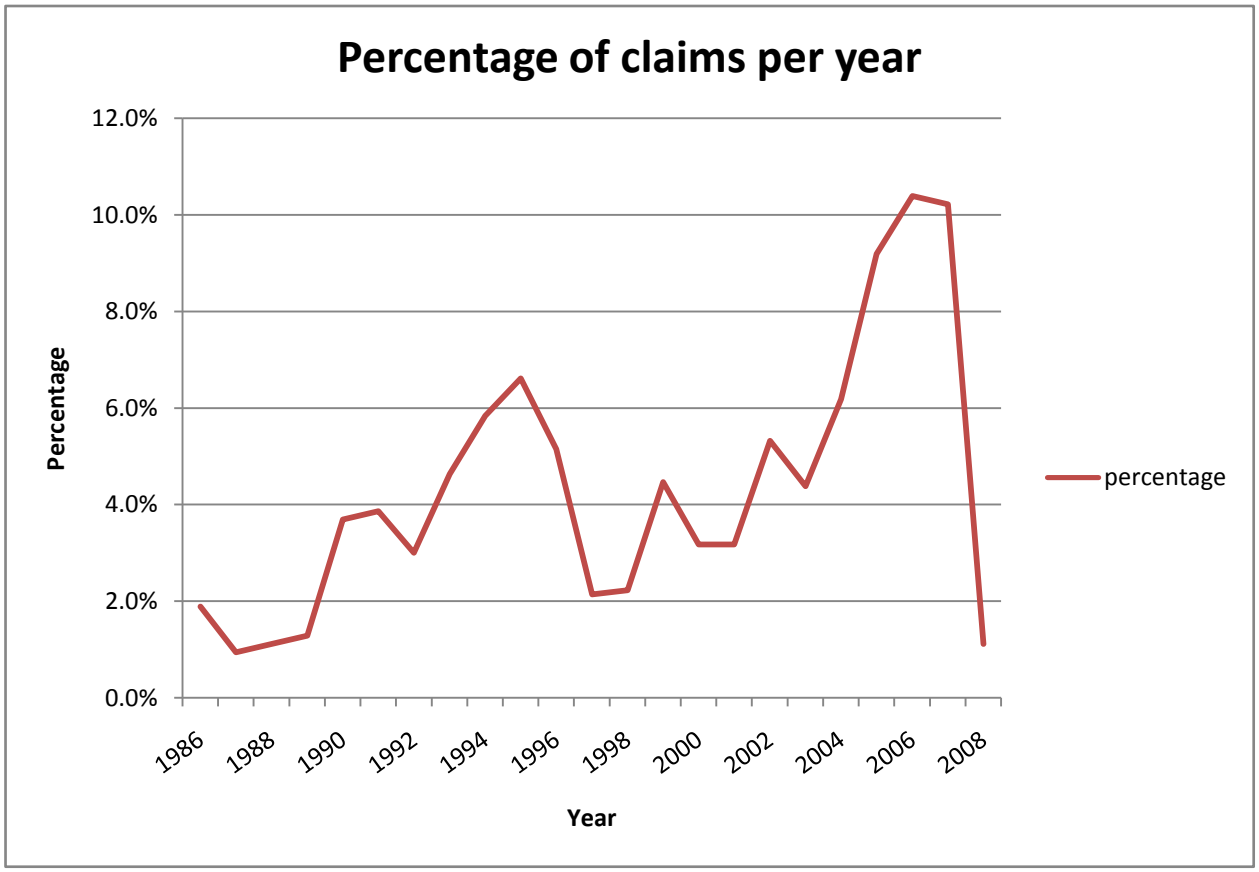

Figure 3: Graph of the number of claims per year (as a percentage)

The following table reflects the percentage of the number of claims per year:

1986	**1987**	**1988**	**1989**	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**
1.9%	0.9%	1.1%	1.3%	3.7%	3.9%	3%	4.6%	5.8%	6.6%	5.2%	2.1%
1998	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	
2.2%	4.5%	3.2%	3.2%	5.3%	4.4%	6.2%	9.2%	10.4%	10.2%	1.1%	

Table 9: Percentage of claims per year

It is evident from both Figure 3 and Table 9 that the number of claims per year and the percentage of claims per year increase with time. This indicates that insurance intermediaries have experienced a steady increase in professional indemnity claims over the past 13 years. It should be noted that the year 2008 is substantially small in value as the data reflects only one quarter of the year.

7.6 Claim description

Of the data, approximately 56% of all the claims provided a detailed description of the claim. From this 56%, the data was sorted according to the claim description.

7.6.1 Per type of claim

The following lists the claim descriptions of the data as well as the percentage of each description:

Claim description	Percentage of data
Breach of mandate	0.3%
Failure to advise	7.4%
Failure to arrange insurance timeously	0.2%
Failure to comply with insured's instructions	0.2%
Failure to notify insurer of material fact	0.6%
Failure to place investments	0.3%
Failure to procure insurance	51.7%
Failure to renew policy	1.1%
Failure to update policy	1%
Fraud by employee	0.2%
Negligence of insured	3.7%
Insurer repudiated claim	17.7%

Claim description	Percentage of data
Misrepresentation	0.6%
Negligence by intermediary	8.7%
Non-disclosure	6.4%

Table 10: Claim descriptions as a percentage of data

The results are graphed below:

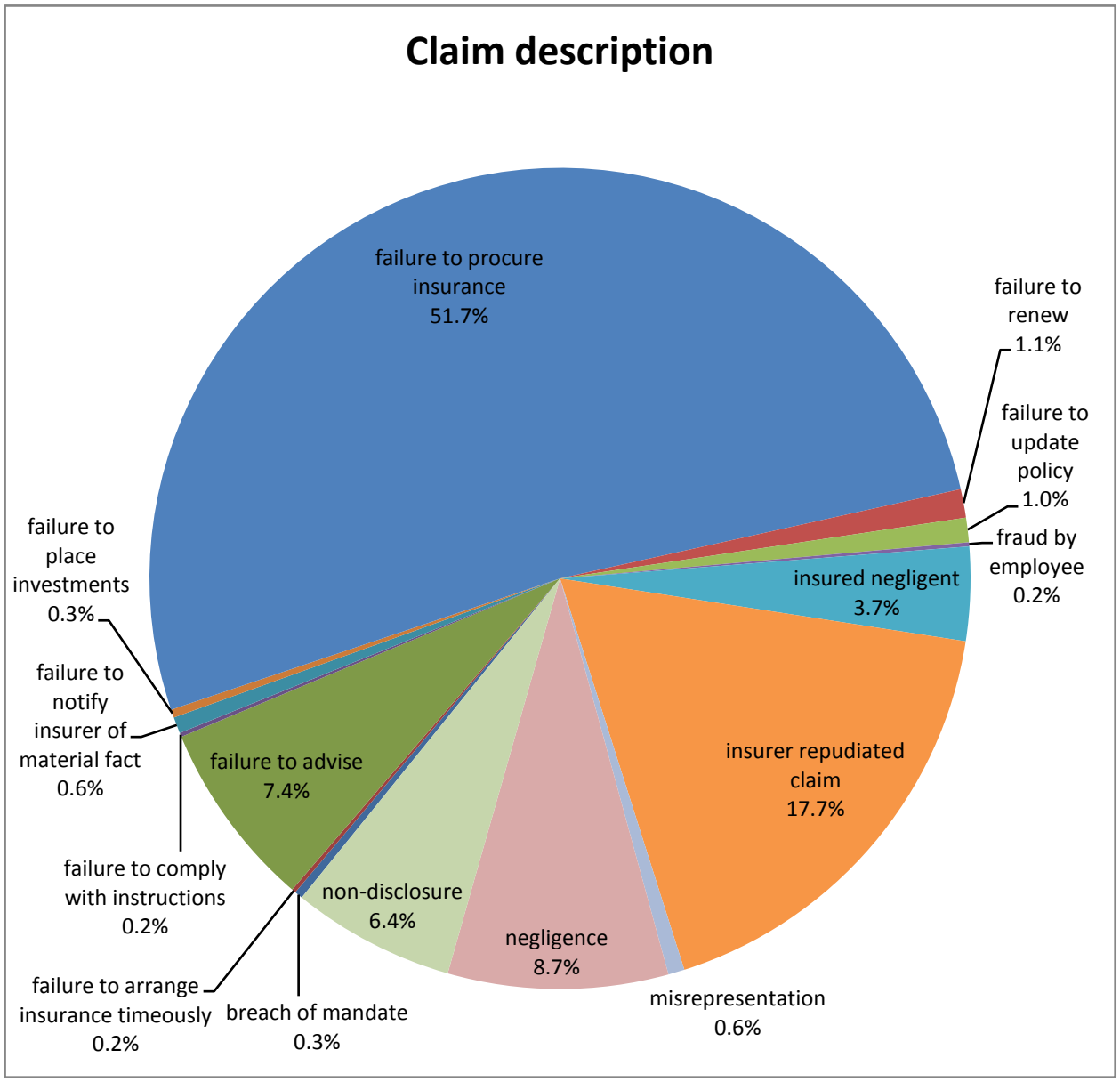

Figure 2: Graph of claim descriptions as a percentage of data

It is evident that the majority of claims, about 52%, were due to the insurance intermediary's failure to procure insurance.

7.6.2 Per year

The following table reflects the claim descriptions by year:

Year	Claim description	Percentage of claim description per year	Percentage of overall per year
1986	Failure to renew	50%	0.3%
	Negligence by intermediary	50%	
1987	Failure to procure insurance	33.3%	0.5%
	Failure to renew insurance	33.3%	
	Negligence by intermediary	33.3%	
1988	Failure to renew	100%	0.2%
1989	Negligence by intermediary	100%	0.2%
1990	Failure to procure insurance	50%	2.6%
	Negligence by intermediary	50%	
1991	Failure to procure insurance	35.7%	2.2%
	Negligence of insured	21.4%	
	Insurer repudiated claim	14.3%	
	Negligence by intermediary	21.4%	
	Non-disclosure	7.1%	
1992	Failure to advise	25%	0.6%
	Failure to procure insurance	25%	
	Negligence by intermediary	25%	
	Non-disclosure	25%	

Year	Claim description	Percentage of claim description per year	Percentage of overall per year
1993	Failure to procure insurance	70.8%	3.9%
	Failure to renew	4.2%	
	Negligence of insured	8.3%	
	Misrepresentation	4.2%	
	Negligence by intermediary	8.3%	
	Non-disclosure	4.2%	
1994	Failure to advise	7.3%	6.6%
	Failure to procure insurance	46.3%	
	Failure to renew	2.4%	
	Failure to update policy	4.9%	
	Negligence of insured	2.4%	
	Insurer repudiated claim	14.6%	
	Non-disclosure	22%	
1995	Breach of mandate	2.1%	7.7%
	Failure to advise	14.6%	
	Failure to notify insured of material fact	6.3%	
	Failure to procure insurance	54.2%	
	Failure to renew	2.1%	
	Insurer repudiated claim	12.5%	
	Non-deposit of premium by intermediary	2.1%	
	Non-disclosure	6.3%	
1996	Failure to advise	5.9%	5.5%
	Failure to procure insurance	79.4%	
	Negligence of insured	5.9%	
	Insurer repudiated claim	8.8%	

Year	Claim description	Percentage of claim description per year	Percentage of overall per year
1997	Failure to procure insurance	92.9%	2.2%
	Insurer repudiated claim	7.1%	
1998	Failure to procure insurance	63.6%	1.8%
	Negligence of insured	9.1%	
	Insurer repudiated claim	9.1%	
	Non-disclosure	18.2%	
1999	Failure to procure insurance	61.5%	4.2%
	Failure to update policy	3.8%	
	Insurer repudiated claim	15.4%	
	Non-disclosure	19.2%	
2000	Breach of mandate	4.3%	3.7%
	Failure to advise	13%	
	Failure to procure insurance	21.7%	
	Insurer repudiated claim	56.5%	
	Non-disclosure	4.3%	
2001	Failure to procure insurance	43.5%	3.7%
	Insurer repudiated claim	52.2%	
	Negligence by intermediary	4.3%	
2002	Failure to advise	12.8%	6.3%
	Failure to comply with insured's instructions	2.6%	
	Failure to procure insurance	23.1%	
	Failure to renew	2.6%	
	Negligence of insured	2.6%	
	Insurer repudiated claim	51.3%	
	Misrepresentation	2.6%	
	Non-disclosure	2.6%	

Year	Claim description	Percentage of claim description per year	Percentage of overall per year
2003	Failure to advise	7.9%	6.1%
	Failure to procure insurance	21.1%	
	Negligence of insured	5.3%	
	Insurer repudiated claim	57.9%	
	Negligence by intermediary	2.6%	
	Non-disclosure	5.3%	
2004	Failure to advise	10.2%	7.9%
	Failure to procure insurance	44.9%	
	Negligence of insured	6.1%	
	Insurer repudiated claim	20.4%	
	Negligence by intermediary	2%	
	Non-disclosure	16.3%	
2005	Failure to advise	11.8%	10.9%
	Failure to place investments	1.5%	
	Failure to procure insurance	41.2%	
	Failure to update policy	2.9%	
	Fraud by employee	1.5%	
	Insurer repudiated claim	2.9%	
	Negligence by intermediary	36.8%	
	Non-disclosure	1.5%	
2006	Failure to advise	6.8%	11.7%
	Failure to procure insurance	71.2%	
	Negligence of insured	4.1%	
	Insurer repudiated claim	5.5%	
	Misrepresentation	1.4%	
	Negligence by intermediary	8.2%	
	Non-disclosure	2.7%	

Year	Claim description	Percentage of claim description per year	Percentage of overall per year
2007	Failure to advise	7%	11.4%
	Failure to arrange insurance timeously	1.4%	
	Failure to place investments	1.4%	
	Failure to procure insurance	66.2%	
	Negligence of insured	7%	
	Insurer repudiated claim	7%	
	Misrepresentation	1.4%	
	Negligence by intermediary	4.2%	
	Non-disclosure	4.2%	
2008	Failure to procure insurance	80%	0.8%
	Negligence of insured	20%	

Table 11: Percentage of claim description per year and overall per year

Table 11 reflects the increase in professional indemnity claims against insurance intermediaries per year, similar to Table 9, however it is based only on that data corresponding to claim descriptions. It further reflects the type of claims against insurance intermediaries per year and indicates that, over the years, insurance intermediaries have experienced a greater variety of the types of claims against them. The failure to procure insurance appears to be the most consistent type of claim each year and accounts for the largest percentage.

8. CONCLUSION

This dissertation focused on examining the legal liabilities of insurance intermediaries and the method of insurance protection available against these liabilities. Within South Africa and abroad, it is evident it is evident that insurance intermediaries are facing increasing liabilities. Particularly in South Africa there has been a substantial increase in the number of claims against intermediaries since 1996.

The scope of liability for insurance intermediaries' seems to be wide ranging, with the courts enforcing decisions at the discretion of the judges; these decisions are based on judicial opinion rather than fact and law. This ultimately expands the scope of liability for which insurance intermediaries are currently being held liable, and will be held liable for in the future.

The increase in the number of claims against intermediaries stems from the fact that insured's are continually seeking other rights of recourse when insurers deny liability. Moreover, in similar instances, insurers may allege that the insurance intermediary is obliged to indemnify the insurer in litigation with an insured.

In South Africa in particular, the dramatic increase in the number of claims against insurance intermediaries further stems from the Ombudsman's ruling since the enactment of FAIS. With no clear jurisdiction, the Ombudsman enforces decisions which are binding, thus furthering the scope of liability of insurance intermediaries.

Previously in South Africa, two main organisations have represented intermediaries: SAFSIA (the South African Financial Advisory & Intermediary Services Association) and IBC (the Insurance Brokers Council). These two organisations however merged to form the Financial Intermediaries Association of Southern Africa (the FIA). Downham (personal communication, September 2009) notes that the new council recognises that the current scheme for members professional indemnity insurance is unsatisfactory which has led to a review of members needs; according to the FIA's figures, its members are responsible for 80% of the short-term market, 60% of the life market, and 80% of the employee benefits market.

Accepted opinion in the market is that the facilities currently available for insurance intermediary professional indemnity insurance do not meet the intermediaries' needs, and the existing 'approved' scheme, which is handled by Marsh (it was previously with Glenrand MIB) is reported to be in disarray as a result of poor administration, and substantial premium increases have been seen (P. Downham, personal communication, September 2009); furthermore SHA

seems to have withdrawn from the market following its merger with Admiral, with the only other major player being Chartis.

Rates (applied to Gross Fee Income) to be charged on PI insurance for insurance intermediaries from a confidential competitor in the market, are as follows:

Limit of Indemnity	**Rate %**
R500 000	0.639
R1 000 000	0.874
R2 500 000	1.054
R5 000 000	1.121
R10 000 000	1.401
R15 000 000	1.682
R20 000 000	1.962

Table 12: Average rating for insurance intermediaries

The rates in Table 12 reflect the average rate based on fee income per limit of indemnity. Average rates were used in the calculation in order to preserve the confidentiality of the competitor.

When calculating ILF's with respect to the above rates, the following procedure was applied, for example to double the limit of indemnity from R500 000 to R1 000 000:

> ([Rate applied to LOI of R1 000 000 – Rate applied to LOI of R500 000] / Rate applied to LOI of R500 000) = Increased limit factor (i.e. percentage of R500 00 premium to be charged to double the LOI)

Therefore the ILF's are as follows:

Increased limit factors			
R500 000 xs R 500 000	R2,5m xs R2,5m	R5m xs R5m	R10m xs R10m
37%	6%	25%	40%

Table 13: Increased limit factors charged by a competitor

It should be noted however that a minimum premium is imposed on limits of indemnity of R500 000 and R1 000 000; this minimum premium increases the rates shown in Table 12. Therefore the ILF to be applied when doubling the limit from R500 000 to R1 000 000 is in fact 46%.

A comparison can thus be conducted between the ILF's for the competitor in the market and those calculated in Section 6 which should theoretically be applied to insurance intermediaries.

Limit of indemnity	**ILF to be charged (Table 5)**	**IFL charged by competitor (Table 13)**	**Difference**	**Loss/Profit by Competitor**
R500 000 xs R500 000	24%	46%	92%	Profit
R2,5m xs R 2,5m	17%	6%	-65%	Loss
R5,0m xs R5,0m	5%	25%	400%	Profit
R10,0m xs R10,0m	3%	40%	1233%	Profit

Table 14: Comparison of increased limit factors

Given the ILF's in Table 13, as compared to those calculated in Table 5 of Section 6, it is evident that insurance intermediaries are being overcharged; most figures stated in Table 13 are significantly higher than those in Table 5. It is evident that although insurers do charge lower rates to higher limits of indemnity, the rates charged are, in most instances, hundreds of times larger than they ought to be.

If it is assumed that the market charges similar rates to those in Table 12, an insurer could stand to gain from the discrepancies in the ILF's as seen in Table 14; should an insurer charge more than the ILF in Table 5 but less than those in Table 13, the insurer will profit as lower rates will be charged giving the insurer a competitive advantage without sacrificing its underwriting standards.

It may well be that the only practical method to protect against the legal liabilities of insurance intermediaries, is insurance. It is clear that the insurance intermediaries market is in need of a suitable product to indemnify insurance intermediaries in situations where they could face potential liability.

9. FUTURE RESEARCH

The scope of future research in line with this dissertation would focus on issues relating to the liabilities and insurance of insurance intermediaries.

With respect to the rating of insurance intermediaries, further research can be conducted in developing an accurate rating model. With the co-operation of the FIA, who dominate and control the insurance intermediary market, a rating model can be developed if underwriting information (such as a breakdown of revenue and claims details) is given to an impartial third party to conduct the research. This information would be of extreme benefit not only to insurers but also to insurance intermediaries themselves, as it would mean that their risks are being correctly rated and insurance to them is charged at appropriate rates. The correct premiums and deductibles to be applied to insurance intermediaries will be value-adding as well as educational to those involved.

As seen in Annexure 4, the Professional Indemnity Section of the insurers' policy provides indemnity for legal liability and the loss of documents. Further research could be conducted in the latter element of cover; that is the liability faced by insurance intermediaries with respect to the loss of documents.

Moreover, Annexure 4 provides four sections of the Insurance Brokers' Professional Insurance Policy, namely Professional Indemnity, Directors' and Officers' Liability, Employment Practices Liability and Fidelity Guarantee. Research may be conducted into each of these additional elements of coverage with respect to insurance intermediaries, above that of a stand-alone PI cover for insurance intermediaries, and the scope and necessity thereof.

Appendix 1 – Specimen International P.I. policy wording

Professional Indemnity Policy

Insurance Brokers

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Welcome

This is **Your** Professional Indemnity **Policy** which has been prepared in accordance with the information **You** have provided

Your Policy, schedule and endorsements together with the **Statement of Fact** should be read together as if they were one document

Please take time to read all these documents to make sure that the cover meets **Your** needs and that **You** understand the terms, exclusions and conditions

If there is anything **You** do not understand or **You** need to change please contact **Your** insurance adviser immediately

This is a legal document and should be kept in a safe place

Your Insurance Policy

This **Policy** is underwritten by certain Underwriters at Lloyd's

We will insure **You** as stated in this **Policy** during the **Period of Insurance** for which **Your** premium has been accepted provided all the terms and conditions of the **Policy** are kept

Where the underwriters are a Lloyd's syndicate they are made up of Lloyd's Underwriters. Each Underwriter is only liable for their own share of the risk and not for any other's share. **You** can ask **Us** for the names of the Lloyd's Underwriters and the share of the risk each has taken

The **Policy**, schedule and endorsements together with the **Statement of Fact** should be read together as if they were one document

You have provided information to **Us** which includes but is not limited to the information detailed in the **Statement of Fact**. **You** agree that all the information provided to **Us** is true and forms the basis of the contract between **You** and **Us**

Law Applicable

In the absence of any agreement in writing to the contrary this **Policy** will be governed by and construed in accordance with the laws of . Any dispute relating to this **Policy** will be subject to the jurisdiction of the courts of .

Definitions

General Definitions

Each time **We** use one of the words or phrases listed below it will have the same meaning wherever it appears in **Your Policy** unless **We** state otherwise. A defined word or phrase will start with a capital letter each time it appears in the **Policy** and is printed in bold type e.g. **Alternate**, except for headings and titles

Throughout this **Policy** words in the singular include the plural and vice versa. The male gender includes the female and neuter. References to legislation include such legislation as amended and to any statutory re-enactment thereof

Alternate
Any individual practitioner partnership limited liability partnership or company who is acting in connection with the arrangements to cover the incapacity or death of a sole practitioner

Binding Authority
any written agreement between **You** and an underwriting or insurance company which delegates authority to **You** to bind business and/ or settle claims on behalf of the said underwriting or insurance company

Claim
The demand by a **Claimant** (including their costs) for compensation or damages or the assertion of a right or rights against **You**

Claimant
Any person or entity making a **Claim**

Computer System
Any computer data processing equipment media or part thereof, or system of date storage and retrieval, or communications system, network, protocol or part thereof, or storage device, microchip, integrated circuit, real time clock system or similar device or any computer software (included but not limited to application software, operating systems, runtime environments or compilers), firmware or microcode

Costs and Expenses
1. Reasonable costs and expenses of **Claimants** for which **You** are legally liable
2. Costs and expenses incurred with **Our** written consent in respect of any **Claim** which may be the subject of indemnity under this **Policy**
3. Fees incurred with **Our** written consent for:
a. defence in any Court of Summary Jurisdiction or on indictment in any higher court in respect of any proceedings brought against **You** in respect of breach or alleged breach of any statutory duty resulting in **Injury**
b. representation at a Coroners Court or Fatal Accident Inquiry in respect of any death in connection with any event which is or may be the subject of indemnity under this **Policy**
Costs and Expenses do not include the costs of work done by **Your** own **Employees** nor any applicable Taxes

Damage
Loss, destruction or damage

Defence Costs
Legal costs and expenses incurred by **You** or on **Your** behalf in the investigation defence and settlement of a **Claim** with **Our** prior written and continuing consent. Defence costs do not include the costs of work carried out by **You** or **Your Employees** nor any applicable Taxes

Document
All forms of document of whatsoever nature which are either the property of or deposited with **You** in connection with the **Professional Business Activity** including **Computer System** records but excluding bearer bonds, coupons, bank notes, currency notes and negotiable instruments

Employee
Any person while working for **You** in connection with the **Professional Business Activity** who is:
1. under a contract of service or apprenticeship with **You**
2. a person who is hired lent or borrowed by **You**
3. a person engaged in connection with a work experience, training or similar scheme
4. a self–employed person working on a labour only basis under **Your** control or supervision

Excess
The amount **You** must pay as the first part of each and every **Claim**

Injury
Bodily injury, death, illness, disease or nervous shock

Investment Business
Any investing of money or capital

Limit of Indemnity
Limit of Indemnity stated in the Schedule

Member
Any member of a limited liability partnership who carries on the **Professional Business Activity** for **You** or on **Your** behalf

Our, Us, We
The Underwriters as set out in the section of the **Policy** headed **Your** Insurance **Policy**

Period of Insurance
The period beginning with the Effective Date shown in the Schedule and ending with the Expiry Date and any other period for which **We** have accepted **Your** premium

Policy
The **Policy** and schedule and any endorsements attached or issued with it

Products
1.Work which has been completed
2.Goods or other material property manufactured, sold, supplied, processed, altered, treated, repaired, serviced, tested, installed, constructed, erected or transported
by **You** or on **Your** behalf in the course of the **Professional Business Activity** and which is no longer in **Your** custody or control

Professional Business Activity
The professional services specified in the **Statement of Fact** by **You** in connection with the **Professional Business Activity** and conducted under **Your** name

Services
Any service performed whilst holding the appointment of Company Secretary, Registrar or Director as referred to in the definition of **Professional Business Activity** includes services performed or advice given by **You** in connection with tax matters, secretarial work, share registration, financial advice to management, book-keeping, management accounting, financial investigation and reports, financial claims - their negotiation and settlement, company formations, investment advice, insurance and pension scheme advice and computer consultancy

Statement of Fact
The proposal form or a statement of facts either in writing or provided electronically and any additional information supplied to **Us** by **You** or on **Your** behalf

You Your Yours
The person people or company named in the Schedule and when requested by **You** the following persons each of whom is severally insured and each of whom agrees that **You** will act on their behalf for all purposes connected with this **Policy** including giving and receiving all notices and agreeing any cancellation or amendment

1.A **Member** and any other person who may during the **Period of Insurance** become a partner or director or **Member**
2.A former partner or director or **Member** including any former partner or director or **Member** whilst acting as a consultant to **You**
3.Anyone who is or has been under a contract of service with **You**
4.Anyone who is or has been under a contract of service with a **Member** but only in respect of any **Claim** arising out of the **Professional Business Activity** carried out on **Your** behalf
5.The estates and/or legal representatives of any person noted under 1,2,3 or 4 above in the event of death, incapacity, insolvency or bankruptcy
6.Any person who is acting on **Your** behalf as an **Alternate**

Policy Conditions

The following Policy Conditions apply to this **Policy** unless otherwise stated

If any term, condition, exclusion or endorsement or part thereof is found to be invalid or unenforceable the remainder will be in full force and effect.

Alteration of Risk
We will not indemnify **You** under this **Policy** if
1. there has been any material alteration in the **Professional Business Activity** or in the occupancy or duties of **You** or **Your Employees** which increases the risk of **Damage** or **Injury** or
2. **Your** interest ceases unless this is brought about by will or operation of law or
3. the **Professional Business Activity** is wound up or carried on by a liquidator or receiver or permanently discontinued unless agreed by **Us** in writing

Cancellation

1. If **You** decide **You** do not want to accept the **Policy** within 14 days of the **Policy** start date in the first year of insurance **You** may cancel this **Policy** by giving notice in writing to **Your** insurance adviser at the address shown in their correspondence or to **Us** at the address shown in the **Policy** quoting **Your Policy** details

In this instance **We** will refund **Your** premium in full provided that there have been no **Claims** made or any **Injury**, **Damage** or consequential loss which could give rise to a **Claim** or circumstance which is likely to give rise to a loss or **Claim** under this **Policy**

This right does not apply to any renewal of this **Policy**

2. **You** may cancel this **Policy** at any other time by giving notice in writing to **Your** insurance adviser at the address shown in their correspondence or to **Us** at the address shown in the Schedule quoting **Your Policy** details

If **You** cancel this **Policy You** may be entitled to the return of a proportionate amount of the premium corresponding to the unexpired **Period of Insurance**. Provided that during the current **Period of Insurance** there have been no **Claims** made or any **Injury**, **Damage** or consequential loss which could give rise to a **Claim** or circumstance which is likely to give rise to a loss or **Claim** under this **Policy**

3. **We** may cancel this **Policy** by sending **You** 30 days written notice to **You** at **Your** last known address

In such event **You** will be entitled to the return of a proportionate amount of the premium corresponding to the unexpired **Period of Insurance**. Provided that during the current **Period of Insurance** there have been no **Claims** made or any **Injury**, **Damage** or consequential loss which could give rise to a **Claim** or circumstance which is likely to give rise to a loss or **Claim** under this **Policy**

4. If the premium has not been paid or if there has been a default under a linked credit agreement this insurance will cease immediately.

In such event **You** may be entitled to the return of a proportionate amount of the premium corresponding to the unexpired **Period of Insurance**. Provided that during the current Period of Insurance there have been no **Claims** made under this **Policy** or any **Injury**, **Damage** or consequential loss which could give rise to a **Claim** or circumstance which is likely to give rise to a loss or **Claim** under this **Policy**

Non Disclosure, Misrepresentation or Misdescription
This **Policy** will be voidable if **You** or anyone acting for **You** fails to disclose, misrepresents or misdescribes any material fact

Observance of Conditions
Your due observance and fulfilment of the terms and conditions of this **Policy** will be conditions precedent to **Our** liability to make any payment under this **Policy**

Premium Payment
You undertake that the **Premium** will be paid in full to **Us** within sixty days of inception of this **Policy** (or, in respect of instalment premiums, when due)

If the premium has not been paid to **Us** by midnight on the premium due date or if there is a default under a linked credit agreement this insurance will cease immediately

Reasonable Precautions
You must
1. exercise care in the selection and supervision of **Alternate , Employees** or **Member**
2. use due diligence and ensure that all reasonable and practicable steps are taken to avoid or diminish any liability
3. comply with all relevant legal requirements, safety regulations and manufacturers recommendations and conduct the **Professional Business Activity** in a lawful manner

Other Insurance
If any **Claim** covered under this **Policy** is also covered by any other **Policy** (or would be but for the existence of this **Policy**) **We** will only indemnify **You** in respect of any excess beyond the amount which would be payable under such other insurance had this **Policy** not been effected

Fraud
If **You** or anyone acting on **Your** behalf makes any false or fraudulent **Claim** or supports a **Claim** by false or fraudulent document device or statement this **Policy** will be void and **You** will forfeit all rights and benefits under this **Policy**. In such circumstances **We** retain the right to keep the premiums and to recover any sums paid by way of benefit under this **Policy**

Subrogation
In the event of any payment under this **Policy** or the notification by **You** of any **Claim** or any **Injury Damage** or consequential loss which would give rise to a **Claim** or circumstance which is likely to give rise to a loss or **Claim We** will be subrogated to all **Your** rights of recovery and **You** will execute all papers required and will do everything necessary to secure and preserve those rights including the execution of documents necessary to enable **Us** to effectively bring proceedings in **Your** name

We agree not to exercise such rights against any company standing in the relationship to subsidiary or of subsidiary to parent to **You** or any company which is a subsidiary to **Your** own parent company current at the time the **Injury Damage** or consequential loss was incurred

We agree not to exercise such rights against any principal partner director **Member** or **Employee** consultant sub-contractor or **Alternate** of **Yours** unless the **Claim** or loss is brought about or contributed to by the dishonest fraudulent criminal or malicious act or omission of that principal partner director **Member** or **Employee** consultant sub-contractor or **Alternate** of **Yours**

Any **Claimant** under this **Policy** will at **Our** request and expense take and permit to be taken all necessary steps for enforcing the rights against any other party in **Your** name before or after any payment is made by **Us**

Claims Conditions

The following Claims Conditions apply to this Policy

1. You will give **Us** written notice within the **Period of Insurance** and in any event within 30 days of when you first became aware of
a. any **Claim** or circumstance which is likely to give rise to a loss or **Claim** including any circumstance likely to give rise to a need to
b. incur mitigation costs
c. the receipt of notice from any party of an intention to make a **Claim**
the discovery that any **Document** has been destroyed damaged lost or mislaid

Where any circumstance is notified during the **Period of Insurance** in accordance with this condition and supplying **Us** with full particulars of the circumstances including the dates and persons involved and the reasons for anticipating a **Claim** or prosecution any later **Claim** or prosecution arising out of the circumstances so notified will be deemed to have been first made at the date of notification

2. You will not
a. admit liability for or settle any **Claim** without **Our** written consent
b. incur any **Defence Costs and Costs and Expenses** in connection with any **Claim** or circumstances which may give rise to a **Claim** without **Our** written consent

In the event that **You** wish to contest a **Claim** which **We** consider should be settled the maximum amount of **Our** liability for that **Claim** will be the amount for which it could be settled plus **Defence Costs** and **Costs and Expenses** down to the date when **We** consider the **Claim** should have been settled subject always to the **Limit of Indemnity**

3. You will
a. use due diligence and ensure that all reasonable and practicable steps are taken to avoid or diminish any liability which may give rise to or has given rise to a **Claim** or loss
b. disclose to **Us** all relevant information and in addition will provide assistance to **Us** to enable **Us** or **Our** agents to investigate and/or defend any **Claim** or loss under this **Policy** and/or enable **Us** to determine **Our** liability under this **Policy**

4. We will be entitled at **Our** expense at any time to take over and conduct in **Your** name the defence investigation or settlement of any **Claim** and to conduct an investigation into circumstances which may give rise to a **Claim** and to receive at all times **Your** full co-operation for this purpose

Allocation

In the event that both indemnity for a **Claim** or loss payable by this **Policy** and liability for a **Claim** or loss not payable by this **Policy** arises either because

a. a **Claim** or a loss against **You** includes both payable and non payable matters; or
b. a **Claim** against **You** is made and others are party to the proceedings or demand to which the **Claim** relates;

then both **You** and **Us** will use their best efforts to agree the allocation of such amount between payable loss and non payable loss based on a fair and proper assessment of the relative legal and financial exposures

Any allocation of **Defence Costs and Expenses** on account of a **Claim** which is negotiated or determined in accordance with this condition will be applied retrospectively to all **Defence Costs and Expenses** on account of such **Claim**

General Exclusions

The following General Policy Exclusions apply to this **Policy** and all Clauses, Extensions and Endorsements unless otherwise stated

We will not be liable for any **Claim** in respect of

1. Sonic Bangs

Damage directly caused by pressure waves caused by aircraft or other aerial devices travelling at sonic or supersonic speeds

2. Radioactive Contamination Nuclear Risks

Damage to any property whatsoever or any loss or expense whatsoever resulting from or arising therefrom or any consequential loss or legal liability of whatsoever nature directly or indirectly caused by or contributed to by or arising from

1) ionising radiation or contamination by radioactivity from any nuclear fuel or from any nuclear waste from the combustion of nuclear fuel
2) the radioactive toxic explosive or other hazardous properties of any explosive nuclear assembly or nuclear component thereof

3. War, Government Action and Terrorism

A. Damage to any property whatsoever or any loss or expense whatsoever resulting or arising therefrom or any consequential loss or any legal liability of whatsoever nature directly or indirectly caused by or contributed to by or arising from
- i. War Government Action or Terrorism
- ii. Civil Commotion in Northern Ireland

B. Legal liability of whatsoever nature or any costs or expenses whatsoever directly or indirectly caused by or contributed to by or arising from War Government Action or Terrorism

War will mean

war, invasion, acts of foreign enemies, hostilities or warlike operation or operations (whether war be declared or not), civil war, mutiny, civil commotion assuming the proportions of or amounting to popular rising, military rising, insurrection, rebellion, revolution, or military or usurped power

Government Action means

martial law, confiscation, nationalisation, requisition, seizure or destruction of property by or under the order of any government or public or local authority or any action taken in controlling preventing suppressing or in any way relating to War

Terrorism means

Any act or acts of any person(s) or organisation(s) involving including but not limited to

- i. the causing occasioning or threatening of harm of whatever nature and by whatever means
- ii. putting the public or any section of the public in fear

in circumstances in which it is reasonable to conclude that the purpose(s) of the person(s) or organisation(s) are wholly or partly of a political religious ideological or similar nature

In any action suit or other proceedings where **We** allege that by reason of this Exclusion as far as it relates to Terrorism any **Claim** is not covered by this insurance the burden of proving such **Claim** is covered will be upon **You**

What is Covered

Insuring Clauses

We will indemnify **You**

1 Legal Liability
against all sums that **You** become legally liable to pay as compensatory damages including **Claimants** costs for any **Claim** first made against **You** during the **Period of Insurance** as a result of any negligent act, negligent error, negligent omission or negligent breach of contract committed by **You** or by any consultant, sub-contractor or agent for whose acts or omissions **You** are liable in connection with the performance of any **Professional Business Activity**

2 Defence Costs
for all **Defence Costs**

3 Loss of Documents
for

(i) any **Claim** first made against **You** and notified in writing to **Us** during the **Period of Insurance** in respect of third party liabilities as a consequence of any **Document** having been destroyed, damaged, lost or mislaid

(ii) or reasonable and necessary costs incurred with **Our** prior written consent in the repair, replacement or reconstitution of any **Document** which during the **Period of Insurance** is discovered and notified in writing to **Us** to have been unintentionally destroyed, damaged, lost or mislaid (and which after diligent search cannot be found)

excluding

a) any loss destruction or **Damage** to computer records caused by the presence of magnetic flux or due to loss of magnetism or defects in the computer records
b) any loss destruction or **Damage** to computer records unless there is physical loss of or **Damage** to the media on which such records were stored
c) any loss destruction or **Damage** of any **Documents** caused by wear tear vermin **Damage** or gradual deterioration

4 Libel and Slander
for any **Claim** in respect of any unintentional libel or slander committed by **You** in the performance of **Your Professional Business Activity**

Limit of Liability

Our aggregate liability under this **Policy** will not exceed the **Limit of Indemnity** inclusive of **Defence Costs**

In respect of Clause 4 Loss of Documents the maximum amount **We** will pay is limited to 5% of the **Limit of Indemnity** in respect of any one **Claim** or series of **Claims** against **You** arising out of one event and in the aggregate in any one **Period of Insurance** which shall be part of and not in addition to the **Limit of Indemnity**

Where **We** are liable to indemnify more than one person company or body the total amount of indemnity payable under this insurance will not exceed the **Limit of Indemnity**

All **Claims** arising out of the same originating cause or source or the same act, error or omission, or series of acts, errors or omissions that are in any way related will be regarded as one **Claim** for the purposes of the **Limit of Indemnity**

What is Not Covered

We will not be liable for

1. the amount of **Excess** shown in the Schedule

2. Any loss or **Claim**

a) arising out of based upon or attributable to any actual or alleged antitrust violation, restraint of trade or unfair competition

b) arising directly or indirectly from **Injury** sustained by any **Employee** or any **Member** arising out of or in the course of his or her employment or for any breach of duty owed to any such person or any person who has made an application for employment with **You** or any **Member**

c) arising directly or indirectly from **Damage** to property, except in respect of loss under Insuring Clause 4

d) for the **Injury** of any person (not being an **Employee** or a **Member**), but this will not apply to any loss or to any **Claim** for psychological injury, emotional distress or anguish or shock which arises from a breach of duty in the performance of (or failure to perform) the **Professional Business Activity**

e) arising from any breach by **You** of a personal duty owed solely in the capacity of a member, director, secretary or officer of a body corporate

f) arising out of, based upon or attributable to any **Binding Authority**, unless specifically covered by this **Policy** or agreed by **Us**

g) made against **You** by any Underwriter or Insurance Company arising out of **Your** activities as their Insurance Agent unless the Underwriter or Insurance Company has obtained a judgment in any court against **You**

h) for taxes, fines or penalties or any **Claim** deemed uninsurable by law

i) arising out of or in any way involving any actual or alleged dishonest, fraudulent, criminal or malicious act or omission by **You** or anyone on **Your** behalf, except in respect of loss under Insuring Clause 3

j) arising out of or relating to **Your** insolvency or bankruptcy other than

a.In respect of monies held on behalf of third parties and/or

b.For which **You** would otherwise be indemnified by this insurance but for **Your** insolvency or bankruptcy

k. arising directly or indirectly from the ownership, possession or use by **You** of land, buildings, mobile or immobile goods or property or vehicles

l. arising out of any circumstance or event which has been notified under any insurance which was in force prior to the **Period of Insurance** or which was known or should have been known to **You** prior to the **Period of Insurance** which might reasonably have been expected to produce a **Claim**

m. arising out of or in connection with any trading losses or trading liabilities incurred by any business managed by or carried on by **You**

n. brought in any court of the United States of America or Canada or anywhere in the world under the laws of the United States of America or Canada or to enforce a judgement first obtained in the courts of or under the laws of the United States of America or Canada or arising from **Professional Business Activity** carried out from any office or other premises in The United States of America or Canada

o. arising out of, based upon or attributable to any allegations that **You** intentionally or negligently permitted, or aided or abetted others in using, was aware of others using, or was a participant or connected in any way in the use of an illegal or improper agreement or other arrangement between an insurance broker and an insurance carrier involving the payment of increased fees, commissions or other compensation based on the volume or type of business referred to the insurance carrier

p. arising out of, based upon or attributable to
i) mechanical failure;
ii) electrical failure, including any electrical power interruption, surge, brown out or black out; or
iii) telecommunications or satellite systems failure

q. arising out of, based upon or attributable to, whether directly or indirectly, the insolvency, administration or receivership of any insurance company, building society, bank, investment manager, stockbroker, investment intermediary, or any other business, firm or company with whom **You** have arranged directly or indirectly any insurance, investment or deposits

r. arising out of or relating directly or indirectly to or in consequence of seepage, pollution or contamination of any kind, save that this exclusion will not apply to any loss or any **Claim** which arises from a breach of duty in the performance (or failure to perform) any **Professional Business Activity**

s. arising out of any **Professional Business Activity** as managers of an insurance company, or underwriting agents

t. arising out of the giving of any express or implied warranty or guarantee relating to the financial return of any investment or portfolio of investments

Appendix 2 – Specimen South African P.I. policy schedule

CERTIFICATE OF INSURANCE

CERTIFICATE NUMBER	:	
MASTER POLICY NUMBER	:	
THE INSURERS	:	
THE UNDERWRITERS	:	
THE INSURED	:	
VAT REGISTRATION NUMBER	:	
THE COMPLIANCE OFFICER	:	
ADDRESS	:	
BUSINESS	:	Insurance Brokers
LIMIT OF LIABILITY -		Annual Aggregate in respect of Insured Events 1,2,3 and 4
PER CLAIM	:	R
PER POLICY PERIOD	:	R
LOSS OF DOCUMENTS LIMIT	:	R 25,000.00 in respect of Replacing or Restoring Documents
CLAIMS PREPARATION COSTS	:	R 50,000.00 Sum Insured
REINSTATEMENT(S)	:	NONE/ ONE / TWO
COVER INCLUDES	:	Professional Indemnity (Insured Event 1)
	:	Staff Dishonesty / Fidelity Guarantee (Insured Event 2)
	:	Loss of Documents Legal Liability (Insured Event 3)
	:	Defence Costs
	:	Defamation and Injuria
EXTENSIONS	:	Compliance Officer (Insured Event 4)
		Computer Crime / Not Applicable
EXCESS EACH AND EVERY CLAIM INCLUDING COSTS AND EXPENSES	:	R5,000.00 but R10,000.00 in respect of Short Term and Investment related Claims. In respect of claims arising from Marine, Aviation and Binding Authority Activities, 2% of Gross Commission (Minimum R15,000.00 and Maximum R75,000.00).
COMPLIANCE OFFICER EXCESS	:	R 7,500
LOSS OF DOCUMENTS EXCESS	:	R 250.00 in respect of Replacing or Restoring Documents
CLAIMS PREPARATION COSTS EXCESS	:	R 7,500
RETROACTIVE DATE	:	
DATE OF PROPOSAL	:	
PERIOD OF INSURANCE	:	From 01/ /200 To: / /200 (both days inclusive)
PREMIUM	:	R (Inclusive of 14% VAT) Per Annum
COMMISSION	:	17.5%

* Wherever Limits of Liability are stipulated within this Policy they are deemed to be inclusive of Vat in terms of the Value-Added Tax Act (Act No 89 of 1991) or as amended.

* THIS SCHEDULE BECOMES A TAX INVOICE WHEN THE TOTAL AMOUNT REQUESTED HAS BEEN PAID. VAT Reg No.4440102095

SIGNED AT JOHANNESBURG THIS DAY OF **200**

AUTHORISED SIGNATORY

Appendix 3 – Specimen South African P.I. policy wording

Professional Indemnity Insurance
For
Intermediaries

(OPTION A)

This is to certify that in accordance with the authorisation granted to (the "Underwriters") by (the "Insurers") and in consideration of, and conditional upon, the prior payment of the Premium by or on behalf of the Insured and receipt thereof by or on behalf of the Insurers, the Insurers are hereby bound to insure in accordance with the terms, Exclusions, Conditions and limitations contained herein or endorsed hereon.

This Insurance Contract is conditional upon and will only come into effect following payment of the premium by the Insured and the receipt thereof by or on behalf of the Insurers.

ADMINISTERED BY

UNDERWRITTEN BY

The Insured having made a written proposal to Insurers, dated as stated in the Certificate, and/or otherwise submitted particulars and statements constituting the risk profile, which proposal and/or risk profile shall form the basis of this insurance, the Insurers will indemnify the Insured in accordance with the terms, Exclusions, Conditions and limitations contained herein or endorsed hereon.

INSURED EVENTS

The Insurers shall indemnify the Insured against losses arising out of:

1. **Professional Indemnity**

Any legal liability arising from claims first made against the Insured and reported to the Underwriters during the Period of Insurance as stated in the Certificate:

for breach of duty in connection with the business by reason of any negligent act, error or omission,

committed in the conduct of the business by the Insured any employee or director or former employee or former director of the Insured, and where the business is or was carried on in partnership any partner or former partner of the Insured.

2. **Fidelity Guarantee/ Employee Dishonesty**

Direct financial losses first discovered, and reported to the Underwriters, by the Insured during the Period of Insurance arising in connection with the Business:

for any direct loss of money or other property whatsoever belonging to the Insured or for which the Insured is legally liable in consequence of any dishonest or fraudulent act or omission of any one employee or any number of employees acting in collusion or independently of each other.

3. **Loss of Documents**

Any legal liability incurred by reason of loss of documents and costs and expenses incurred in replacing or restoring such documents.

PROVISOS TO INSURED EVENTS 1,2,3 AND 4 (ONLY WHERE SUCH INSURED EVENTS ARE COVERED AND UNLESS OTHERWISE STATED)

(i) the Insurers shall not indemnify any employee committing, making or condoning any dishonest or fraudulent act or omission;

(ii) for the purposes of Insured Event 2, "employee" shall not include a director of a corporate Insured owning more than 20% of the equity of the Insured and "former employee" shall be construed accordingly;

(iii) the Insured shall give immediate notice to the Insurers where there is any reasonable suspicion of fraud or dishonesty being committed by any employee whether giving rise to a claim or not under this Policy;

(iv) the Insurers shall be entitled to pursue recovery of all monies paid or payable under this Policy against the employees concerned or their estates or personal representatives or trustees or assignee in bankruptcy;

(v) the Insured shall provide all reasonable information and assistance requested by the Insurers in pursuance of such recovery and shall in particular withhold monies due to or held by the Insured but belonging to the dishonest or fraudulent employee or employees, their estates or personal representatives or trustee or assignee in bankruptcy for the benefits of the Insured but only to the extent of the loss which they have suffered or will suffer as a result of the said employees dishonesty;

(vi) the Insured shall whenever requested by the Insurers take all necessary steps for prosecuting or convicting employees for dishonest acts;

(vii) for the purposes of Insured Event 3, the amount of any claim for costs and expenses incurred in replacing or restoring any documents shall be supported by bills and accounts which shall be subject to approval by a competent person nominated by the Insurers;

(viii) for the purposes of Insured Event 4, the Compliance Officer is an Employee of the Insured and Exclusion 12 shall not apply up to 50% of the Limit of Liability stated on the Certificate or R1,000,000 whichever is the lesser.

DEFENCE COSTS **(and ancillary claims costs)**

Insurers will pay legal and other costs and expenses incurred with their written consent in the defence and/or settlement of any claim.

The above costs will be part of, and not in addition to the limit stated in the Certificate.

Costs and expenses incurred in successful defence will also be deemed to be a claim in terms of the policy and therefore subject to the excess as stated in the Certificate.

LIMIT OF LIABILITY

The total liability of the Insurers, in terms of the Insured Events:

(a) Per Claim or series of claims arising from one originating cause or source, including interest thereon, all claimants' costs, fees and expenses and Defence Costs;

(b) in respect of all claims Per Policy Period;

shall not exceed in the aggregate, in respect of Defined Events 1,2,3, 4 and 5 and 4 the Limit of Liability stated in the Certificate.

DEFINITIONS

1. THE INSURED

(1) as stated in the Certificate,

(2) their predecessors in business,

(3) their Subsidiaries as may currently exist or hereinafter be created and/or companies under the management control of the Insured,

(4) any person at any time employed by the Insured including any persons seconded from other companies or consultants or representatives of the Insured whether remunerated by salary or commission or otherwise,

(5) any other agreed Company or agreed person with whom the Insured is or has been acting or any person at any time employed by such agreed company or agreed person,

(6) any future, current or former director of the Insured,

(7) any future, current or former employee,

(8) the estate, heirs or legal representatives or trustees or assignees of any party entitled to indemnity following their death, incapacity, insolvency or bankruptcy.

2. EMPLOYEE

It is agreed and understood that the word "Employee" wherever used in the Policy or in any additional Endorsement means :-

i. any person engaged under a contract of employment with the Insured;

ii. any guest student pursuing studies or duties with the Insured when so acting;

iii. any person provided by an employment contractor or agency to perform employee duties for the Insured under the Insured's supervision;

iv. any person or entity authorised by the Insured to perform services as data processor of cheques or other accounting records of the Insured; each such person or entity, and the partners, officers and employees thereof, shall collectively be deemed to be one employee;

v. any person remunerated by the Insured on a commission only basis; however cover shall only extend to indemnify the Insured in respect of acts undertaken by such persons for and on behalf of the Insured.

NOTE: The phrase "former employee" shall be construed in the contents of (i) to (v) above.

3. SUB AGENTS

This Insurance extends to indemnify the Insured in respect of the professional activities and duties necessary to carry out the Business/Profession, and which are sub contracted by the Insured, provided always that:

a) such activities and duties shall only be sub-contracted to suitably qualified firms, persons or parties;

b) the Insured shall at all times retain all rights of recourse against such firms, persons or parties and will give all reasonable assistance to the Insurers in effecting such rights.

4. THE DOCUMENTS

Any documents (whether on paper, microfilm, magnetic tape or disc), including films, tapes, deeds, wills, agreements, maps, plans, drawings, abstracts, mortgage agreements, manuscripts, records (including books, letters, certificates), either the property of or entrusted to the Insured or in the custody of any person to or with whom such documents have been entrusted, lodged or deposited by the Insured.
The documents do not include bearer bonds, coupons, bank notes, currency notes and negotiable instruments.

5. BUSINESS

"Business" means all professional activities of the Insured including

a) Insurance and Life Assurance/Broking
b) Pensions Broking and Administration
c) Mortgage Broking and Building Society Agency Activities
d) Investments in insurance Bonds
e) Investments in Unit Trusts
f) Dealing in listed Securities
g) Dealing in unlisted Securities
h) Dealing in Foreign Securities/investments
i) Dealing in Bonds
j) Dealing in Commodities (futures or physicals)
k) Investment in "Tangibles"
l) Private client portfolio management
m) Institutional fund management
n) Corporate Finance, including leasing investment schemes
o) Business Expansion Scheme Placings
p) Health Care Products.

6. EXCESS

shall mean that first amount of each and every claim to be borne by the Insured, it being understood and agreed that if any expenditure is incurred by the Insurers which, by virtue of the Excess, is the responsibility of the Insured, then such expenditure shall be forthwith reimbursed by the Insured.

The Excess shall apply Per Claim or series of claims arising from one originating cause or source.

7. PROFESSIONAL DUTIES– COMPLIANCE OFFICER

"Professional Duties" shall mean the duties of the Compliance Officer as contemplated and further defined in the Financial Advisory and Intermediary Services Act 2002 (as amended) and shall also extend to include any responsibility assumed by the Compliance Officer to ensure the Insured's compliance with the Financial Intelligence Centre Act 2001 (as amended).

EXCLUSIONS

The Insurers shall not indemnify the Insured in respect of any loss arising out of any claim made against them

1. resulting from
    a) the failure to account for monies or securities in lieu of such monies
    b) the financial failure of any Insurer
    c) death, bodily injury or damage to property unless arising from a negligent act, error or omission to perform a professional duty;

2. by any Underwriter or Insurance Company unless that Underwriter or Insurance Company has obtained a judgement in any court against the Insured in respect of such claim;

3. resulting from the Insured's activities as Underwriters, Underwriting Agents or Managers of any Insurance Company, Underwriter or syndicate of Underwriters where the Insured is a risk carrier;

4. (i) resulting from any circumstance or occurrence which is either

    a) known to the Insured at the inception of this Policy and likely to give rise to a claim against which the Insured would otherwise be entitled to be indemnified or
    b) which has been notified under any other insurance attaching prior to the inception of this Policy

    (ii) in respect of any third party claim arising from or contributed to by depreciation (or failure to appreciate) in value of any investments, including securities, commodities, currencies, options and futures transactions, or as a result of any actual or alleged representation, guarantee or warranty provided by or on behalf of the Insured as to the performance of any such investments.
    It is agreed however that this Exclusion shall not apply to any loss due solely to negligence on the part of the Insured or Employee of the Insured in failing to effect a specific investment transaction in accordance with the specific prior instructions of a client of the Insured.

5. by any Parent or Subsidiary Company of the Insured or by any Company or entity in which the Insured or directors or officers of the Insured have a controlling interest unless such claim emanates from an independent third party;

6. for which they are entitled to indemnity under any other Policy;

7. arising from breach of contract unless such breach is a breach or alleged breach of professional duty by the Insured or any other person upon whom the Insured has placed reliance;

8. from the conduct of the business in the United States of America and/or Canada, and/or following from any judgement, award, payment, or settlement made within countries which operate under the laws of the United States of America or Canada (or to any order made anywhere in the world enforcing such judgement, award payment or settlement, either in whole or in part) as a result of any actual or alleged negligent act error or omission in the performance of the professional duties of the Insured in accordance with the Business;

9. for any legal liability, loss, damage, cost or expense whatsoever or any consequential loss directly or indirectly caused by or contributed to by or arising from:

    a) ionising radiations or contamination by radioactivity from any nuclear fuel or from any nuclear waste from the combustion or use of nuclear fuel;
    b) nuclear material, nuclear fission or fusion, nuclear radiation;
    c) nuclear explosives or any nuclear weapon;
    d) nuclear waste in whatever form;

    regardless of any other cause or event contributing concurrently or in any other sequence to the loss. For the purpose of this Exclusion only, combustion shall include any self-sustaining process of nuclear fission;

10. for computer crime resulting directly from a fraudulent

    i) entry of data into or
    ii) change of data elements or programs within the Insured's proprietary computer system or a computer system , provided the fraudulent entry or change causes

        a) property to be transferred, paid or delivered
        b) an account of the Insured, or its customer, to be added, deleted, debited or credited, or
        c) an unauthorised account or a fictitious account to be debited or credited;

11. up to the amount of the Excess;

12. for fines, penalties, punitive, vindictive or exemplary damages.

SPECIAL EXCLUSIONS

1. COMPUTER VIRUS EXCLUSION

   Notwithstanding any provision of this Policy including any special Exclusion or extension or other provision not included herein which would otherwise override a general Exclusion, this Policy does not cover any legal liability of whatsoever nature directly or indirectly caused by or contributed to by or consisting of or arising from the incapacity or failure of any computer, correctly or at all, to capture, save, retain or to process any data as a result of the action of any computer virus, or other corrupting, harmful or otherwise unauthorised code or instruction including any trojan horse, time or logic bomb or worm or any other destructive code, media or programme or interference.

   A computer includes any computer, data processing equipment, microchip, integrated circuit or similar device in computer or non-computer equipment or any computer software, tools, operating system or any computer hardware or peripherals and the information or data electronically or otherwise stored in or on any of the above, whether the property of the Insured or not.

2. WAR / TERRORISM EXCLUSION

   The Insurers shall not be liable to indemnify the Insured in respect of claims directly or indirectly caused by, resulting from happening through or in connection with:

   a) war, invasion, act of foreign enemy, hostilities or warlike operations (whether war be declared or not), civil war, mutiny, insurrection, rebellion, revolution, military or usurped power;

   b) any action taken in controlling, preventing, suppressing or in any way relating to the excluded situations in a) above, including, but not limited to, confiscation, nationalization, damage to or destruction of property by or under the control of any Government or Public or Local Authority;

   c) any act of terrorism regardless of any other cause contributing concurrently or in any other sequence to the loss.

      For the purpose of this Exclusion, terrorism means an act of violence or any act dangerous to human life, tangible or intangible property or infrastructure with the intention or effect to influence any government or to put the public or any section of the public in fear.

   In any action suit or other proceedings where the Insurer alleges that by reason of this Exclusion a loss is not covered by this insurance the burden of proving that such loss is covered shall be upon the Insured.

3. ASBESTOS EXCLUSION

   Notwithstanding any provision of this Policy including any Exclusion, exception or extension or other provision which would otherwise override an Exclusion, this Policy does not cover any legal liability, loss, damage, cost or expense whatsoever or any consequential loss directly or indirectly caused by, arising out of, resulting from, in consequential of, in any way involving, or to the extent contributed to by, the hazardous nature of asbestos in whatever form or quantity.

CONDITIONS

1. The due observance and fulfilment of the terms, conditions and endorsements of this Policy by the Insured shall be a condition precedent to any liability of the Insurers to make any payment under this Policy.

2. The Insured shall give to the Insurers notice as soon as reasonably possible in writing of any claim made upon them or of any occurrence of which they become aware which may subsequently give rise to a claim and if during the subsistence of this Policy the Insured shall give such notice then any such claim or claims which may subsequently be made by or against them arising out of the said claim or occurrence shall for the purpose of this Policy be deemed to have been made during the subsistence hereof.

3. Notification by the Insured within 30 days of the expiry of this Policy of any claim being made against the Insured, or of any specific event or circumstance likely to give rise to a claim being made against the Insured, but only in respect of indemnifiable events in terms of this Policy committed or occurring prior to such expiry, shall be dealt with as if the claim had been made against the Insured during the Period of Insurance.

4. Upon request the Insured shall give to the Insurers for the settlement or defence of a claim all such information and assistance as the Insurers may reasonably require and as may be in the Insured's power and will in all such matters do and concur in doing all such things as the Insurers may require.

5. The interpretation and enforcement of the terms, Conditions and Exclusions of this Policy (and any phrase or word contained herein) shall be in accordance with the law of the Republic of South Africa whose courts shall have jurisdiction to the exclusion of the courts of any other country.

6. The Insured shall not make any admission, offer, promise, payment or indemnity for any claim or incur any expenses in connection therewith without the written consent of the Insurers.

7. The Insured shall not be required to contest any legal proceedings unless Senior Counsel (to be mutually agreed upon by the Insured and the Insurers) shall advise that on the actual facts of the case concerned such proceedings can be contested by the Insured with a reasonable prospect of success.

8. No claim shall be payable in the event of an action or suit not being instituted by the Insured against the Insurer within 90 days following the rejection or disclaimer of liability by the Insurer.

9. If the Insured shall make any claim knowing the same to be false or fraudulent, as regards the amount or otherwise, this Policy shall become void and the Insured shall forfeit all benefits hereunder.

10. In the event of the Insurers being at any time entitled to avoid this Policy by reason of any inaccurate or misleading information given by the Insured in the proposal form, Insurers at their discretion, instead of avoiding this Policy, may give notice in writing to the Insured that they regard this Policy as of full force and effect save that there shall be excluded from the indemnity afforded hereunder any claim which has arisen or which may arise and which is related to circumstances which ought to have been disclosed in the Proposal Form to Insurers.

    This Policy shall then continue in full force and effect but shall be deemed to exclude, as if the same had been specifically endorsed, the particular claim or possible claim referred to in the said notice.

ENDORSEMENTS

1) BASIS OF VALUATION

It is agreed that the value of any securities or foreign funds or currencies for the loss of which a claim shall be made shall be determined by their closing market value on the last business day prior to the date of discovery of the loss or, in the event of the discovery of the loss after the close of the market, by their closing market value on the day of discovery of the loss.

If there is no market price or value for the same on the day as stated in the preceding paragraph then the value shall be as agreed between the Insured and the Underwriters or in default thereof by arbitration. If, however, such securities or foreign funds or currencies shall be replaced by the Insured with the approval of the Underwriters, the value shall be the actual cost of replacement.

2) WAIVER OF SUBROGATION

It is agreed that the Insurers, upon payment of any loss under this Policy or any other applicable Endorsement, shall become subrogated to all rights and remedies of the Insured in respect of such loss. However, notwithstanding anything in the Policy or any other Endorsement to the contrary :-

Insurers agree to waive any rights of subrogation against any Employee of the Insured except in respect of any liability arising from or contributed to by any dishonest, fraudulent, criminal or malicious act or omission on the part of any such employee.

3) INDIVIDUAL APPOINTMENTS

This Policy and all other applicable Endorsements are extended to indemnify the Insured and any past or present principal, director or officer of the Insured against losses arising from claims first made against any of them during the Period of Insurance whilst acting as a director, secretary, trustee, manager or registrar of any company or entity other than the Insured and Subsidiary companies of the Insured, where such position is held by reason of the Insured's Business and provided that any fees received from such appointment form part of the income of the Insured.

4) JOINT VENTURE APPOINTMENTS

Insurers agree that the indemnity provided under this Policy shall extend to include all liability of the Insured arising out of any Joint Venture Agreement the Insured may enter into with any other party or parties provided always that:

1. No separate indemnity, other than that provided for under this Certificate, has been arranged for the benefit of the Insured under the Joint Venture Agreement.

2. Insurers shall be entitled to exercise any rights of recourse in respect of loss indemnified hereunder which rights vest in the Insured by virtue of the Joint Venture Agreement.

5) NEW AND/OR ACQUIRED COMPANIES

This Policy extends to indemnify any new and/or acquired Subsidiary company, subject to full satisfactory details being lodged with Insurers as soon as practicable and subject to the exclusion from this Policy of any claim or circumstance known to the Insured and/or such Subsidiary company at the date cover attaches hereto and further subject to an additional premium to be agreed by Insurers if required.

6) CLAIMS PREPARATION COSTS

Notwithstanding anything to the contrary contained in the Policy, it is understood and agreed that the Policy is extended to include costs reasonably incurred by the Insured in producing and certifying any particulars or details required to substantiate the amount of any loss, subject to the Sum Insured and Excess specified in the Certificate.

7) BREACH OF CONFIDENTIALITY

This Policy shall indemnify the Insured for any claim or claims made against them howsoever arising out of unintentional Breach of Confidentiality.

8) RETROACTIVE DATE

The company shall not be liable to provide indemnity hereunder for any events which occurred prior to the Retroactive Date stated in the Certificate, provided that nothing contained within this Endorsement shall be interpreted as releasing the Insured from their obligation to reveal as material fact all details of Claims made or outstanding or events likely to give rise to a claim.

In the event that the Limit of Liability is increased, the Retroactive Date applicable to this increased Limit of Liability will be the effective date of said increase.

9) MONTHLY POLICIES - INSTALMENT PREMIUMS

(a) The Monthly Premiums payable to Insurers are in respect of the Annual Period of Insurance as stated in the Certificate of Insurance.
Should any Monthly Premiums be debited to the Insured and/or paid to the Insurers in respect of any period subsequent to the Annual Period of Insurance and Insurers have not confirmed renewal, then no liability shall attach to the Insurers and such Premiums debited or paid shall be refunded to the Insured.

(b) In consideration of the Underwriters / Insurers having agreed, at the request of the Insured, to allow the Insured to pay the Annual Premium by monthly instalment, the Insured accepts and agrees to the following:-

(1) the monthly instalment shall be payable 30 days in arrears to Underwriters / Insurers,

(2) in the event of the Underwriters / Insurers not receiving the instalment for any reason whatsoever, this Insurance shall, notwithstanding anything to the contrary contained in the policy, be deemed to have been cancelled on the last day of the last month for which an instalment was received by Underwriters / Insurers.
Reinstatement of this Insurance shall be at the sole discretion of the Underwriters / Insurers, but Underwriters / Insurers shall not unreasonably withhold such reinstatement provided the Insured can give explanations acceptable to the Underwriters / Insurers for the failed payment,

(3) in the event of prior notification of any claim or circumstances that might lead to a claim during the Annual Period of Insurance for which an unpaid monthly instalment premium applies, Underwriters / Insurers reserve the right to cease all activity on such claim or circumstance and any outstanding matters will be the responsibility of the Insured. Should payments have been made by Underwriters / Insurers on any claims then such payments may be reclaimed from the Insured.

Subject otherwise to the Terms, Exclusions, Conditions and limitations of the Policy.

10) PENSION TRUSTEES

This Policy is extended to indemnify the Insured, and any Partner, Officer, Director or employee of the Insured against any claim for breach of duty which may be made against them by reason of any negligent act, error or omission committed in their capacity as Trustees of Pension Funds.

11) DEFAMATION AND INJURIA

The terms negligent act, error or omission are deemed to include defamation, including injurious falsehood.

12) CANCELLATION

It is hereby understood and agreed that this contract can be cancelled by Underwriters by giving 30 days notice in writing to the Insured via- any media available at the time, including but not limited to Fax, E-mail and Mail.

13) COMPLIANCE OFFICER

Insured Event 4 shall not apply where the Compliance Officer is also the Insured and where the Professional Duties of a Compliance Officer are also performed by the Insured in the course of the Insured's Business.

The above Endorsements are subject to the terms, Exclusions, Conditions and limitations of the Policy.

EXTENSIONS

The following Extensions will apply only if stated in the Certificate to be included and

a) shall be subject to the relevant Limits of Liability and Excesses applicable to the Extensions
b) are subject otherwise to the terms, Exclusions, Conditions and limitations of the Policy;

PROVIDED ALWAYS THAT, in respect of all Extensions, the total liability of the Insurers is not increased beyond that which would have applied in the absence of such Extensions.

1. **Compliance Officer (Insured Event 4)**

   The Insurers shall indemnify the Compliance Officer against his liability to pay compensation (including claimants' costs, fees and expenses) to the Insured and any other third party as a result of any actual or alleged (other than by the Compliance Officer) negligent act, error or omission (including consequential loss) in the performance of the Professional Duties of the Compliance Officer undertaken in the course of the Insured's Business.

2. **Third Party Computer Crime (Insured Event 5)**

   Notwithstanding Exclusion No 10, this Policy extends to indemnify the Insured in respect of loss resulting from a fraudulent

   (i) entry of data into or
   (ii) change of data elements or programs within the Insured's proprietary computer system or a computer system, provided the fraudulent entry or change causes
      a) property to be transferred, paid or delivered
      b) an account of the Insured, or its customer, to be added, deleted, debited or credited, or
      c) an unauthorised account or a fictitious account to be debited or credited.

Appendix 4 – Specimen South African combined P.I., D&O, E.P.L. and F.G. policy wording

GENERAL OPERATIVE CLAUSE

The Insured named in the Schedule having applied to the Underwriters for the Insurance and having agreed that any proposal or other information supplied by the Insured or on his behalf shall be the basis of this contract of insurance, the Underwriters agree, in consideration of the payment of the premium, to bind themselves to indemnify the Insured as provided for within the Insuring Agreements of each Section of this Policy subject to the terms, Exclusions and Conditions of this Policy.

Authorisation Clause

By acceptance of this Policy, all persons, companies and other entities insured hereby agree that the party named as the Insured in the Schedule will act on behalf of all the insureds in respect of the giving and receiving of notice of claim or termination of cover, the payment of premiums and the receiving of any return premiums that may become due under this Policy, the agreement to and acceptance of endorsements, and the giving or receiving of any notice provided for in this Policy.

GENERAL EXCLUSIONS

This Policy shall not indemnify the Insured or any person or entity insured in terms of this Policy in respect of any claim, loss, liability or expense arising directly or indirectly out of :-

1. Asbestos and Toxic Mould

or in any manner related to, asbestos and Fungi.
For the purposes of this clause, Fungi shall mean any fungus or mycota or any by-product or type of infestation produced by such fungus or mycota, including but not limited to mould, mildew, mycotoxins, spores or any biogenic aerosols.

In any claim and in any action, suit or other proceedings to enforce a claim under this Policy, the burden of proving that such claim does not fall within this Exclusion shall be upon the Insured.

This Exclusion does not apply in respect of any claim, Loss, liability or expense, arising directly or indirectly out of the negligent failure of the Insured to place insurances on behalf of clients for the above named events, or any other breach of professional duty, by the Insured or any person or firm acting on behalf of the Insured.

In the event that any portion of this Exclusion is found to be invalid or unenforceable, the remainder shall continue to be in full force and effect.

2. Claims and Circumstances known at inception

any Claim or Circumstance known to the Insured prior to the inception of this Policy or which in the reasonable opinion of the Underwriters ought to have been known to the Insured

3. Nuclear Risks and War/Terrorist Risks

or caused by or contributed to by

3.1 ionising radiations or contamination by radioactivity from any nuclear fuel, waste or substance or

3.2 the radioactive, toxic, explosive or other hazardous properties of any explosive, nuclear assembly or nuclear component thereof

3.3 war, invasions, acts of foreign enemies, hostilities (whether war be declared or not), civil war, rebellion, revolution, insurrection, riot, civil commotion assuming the proportion of or amounting to a popular uprising, military or usurped power or confiscation or nationalisation or requisition or destruction of or damage to property by or under the order of any government or public or local authority, or

3.4 any act or acts, or threat thereof, of terrorism, force or violence for political, religious or other ends directed towards the overthrowing or influencing of the government, or for the purpose of putting the public in fear, by any person or persons acting alone or on behalf of or in connection with any organisation.

In any claim and in any action, suit or other proceedings to enforce a claim under this Policy, the burden of proving that such claim does not fall within this Exclusion shall be upon the Insured.

In the event any portion of this Exclusion is found to be invalid or unenforceable, the remainder shall continue to be in full force and effect.

This Exclusion does not apply in respect of any claim, Loss, liability or expense arising directly or indirectly out of the negligent failure to place insurances on behalf of clients for the above named events, or any other breach of professional duty by the Insured.

4. Pollution

based upon or attributable to

4.1 the actual, alleged or threatened discharge, release, escape, seepage, migration or disposal of pollutants into or on real or personal property, water or the atmosphere; or

4.2 any direction or request that the Insured, or any person or entity to whom indemnity is extended, to test for, monitor, clean up, remove, contain, treat, detoxify or neutralise pollutants, or any voluntary decision to do so; based upon, arising out of, or attributable to the matters described in this exclusion;

This Exclusion does not apply in respect of any claim, Loss, liability or expense, arising directly or indirectly out of the negligent failure of the Insured to place insurances on behalf of clients for the above named events, or any other breach of professional duty, by the Insured or any person or firm acting on behalf of the Insured.

5. Punitive or Exemplary Damages

any fines, penalties, punitive or exemplary damages imposed on any Insured.

6. Retroactive Date

any act, error, omission or Wrongful Act committed or alleged to have been committed prior to the Retroactive Date (if any applicable) specified in the Schedule.

DEFINITIONS AND INTERPRETATIONS

Various words and phrases have a standard meaning within this Policy and such meanings are defined in this section. Where a more general meaning applies this will be apparent from the way it is used in this Policy.

In any instance where there is conflict, Specific conditions shall override General conditions.

The titles and headings to the various paragraphs and sections in this Policy, including endorsements attached, are included solely for ease of reference and do not in any way limit, expand or otherwise affect the provisions of such paragraphs and sections to which they relate.

Circumstance means:

an event, or series of events arising out of one originating cause, which gives, or is likely to give, rise to a Claim or Claims against any Insured and /or is the subject of indemnity provided under this Policy.

Defence Costs mean:

all costs, charges, fees (including but not limited to attorneys' fees and experts' fees) and expenses incurred with the prior written consent of the Underwriters (which consent shall not be unreasonably withheld) in the investigation, defence or negotiation of the settlement of any Claim.

Defence Costs do not include the overheads of the Insured, including but not limited to the salaries, wages or benefits of any of its directors, officers, Employees, in-house lawyers or other in-house professional advisers.

In relation to the Employment Practice Liability Section, if the service provider named in the Schedule is not utilized by the Insured, the Underwriters shall not be liable for costs and expenses exceeding the amounts in the following table

ACTIVITY	RATE
Consultation	R500 per hour
Preparation for CCMA	R500 per hour
Attendance at Conciliation	R500 per hour
Attendance at Arbitration	R3 500 per day
Labour Court Work	R1 000 per hour

Moreover, Defence Costs shall not include:

1. the cost of conducting disciplinary hearings;
2. the cost of conducting pre-dismissal arbitrations unless the Underwriters give their prior written consent to such arbitration taking place

The First Amount Payable does apply to Defence Costs.

Limit of Indemnity means:

the sum stated in the Schedule which is the maximum amount applicable to any and all Claims, inclusive of all costs and expenses including Defence Costs, for which indemnity is provided under this Policy. The Underwriters' aggregate liability during the Period of Insurance shall not exceed the Limit of Indemnity.

Policy means:

the contents of this document together with the Schedule, incorporating all Extensions and Endorsements, issued from time to time by the Underwriters to attach to this insurance together with the Proposal which shall all be read together as evidencing the contract of insurance.

Period of Insurance means:

the period stated in the Schedule.

Pollutants means:

any substance located anywhere in the world exhibiting any hazardous characteristics as defined by or identified on a list of hazardous substances issued by any governmental agency in the country where this Policy is issued. Such substances shall include, without limitation, solids, liquids, gaseous or thermal irritants, contaminants or smoke, vapor, soot, fumes, acids, alkalis, chemicals or waste materials. Pollutants shall also mean any other air emission, odour, waste water, oil or oil products, infectious or medical waste, asbestos or asbestos products, electric or magnetic or electromagnetic field and noise.

Professional Business means:

the Insured's business activities as insurance brokers on behalf of third party Underwriters and any other business as may be specifically stated in the Schedule or any Endorsement, agreed by the Underwriters, to this Policy.

Proposal means:

the application for the insurance cover provided by this Policy including the proposal form identified in the Schedule together with any other documentation or information submitted to the Underwriters for consideration of the risk.

First Amount Payable means:

The amount stated in the Schedule as the First Amount Payable to be borne by the Insured / Company or Insured Person, as the case may be, and Underwriters shall only be liable for the amount of Loss arising from a claim against this Policy which is in excess of the First Amount Payable which shall remain uninsured.

Schedule means:

The Schedule attaching to this Policy, incorporating all Endorsements.

Subsidiary means:

any organisation in which the Parent Company either directly or indirectly through one or more of its subsidiaries:

1. holds more than 50% of the issued share capital; or

2. has the right to appoint or remove a majority of its board of directors; or

3. controls alone, pursuant to a written agreement with other shareholders, more than 50% of the voting rights therein.

4. any Company other than those referred to in 1, 2 or 3 above in respect of which the Underwriters have given prior written consent to its coverage as a subsidiary Company under this Policy.

Takeover or Merger means:

any transaction whereby another company acquires control over the assets or management of the named Insured or whereby the assets of the Insured become vested in or under the control of another company including a transfer of whole or any part of a business, trade or undertaking that is transferred as a going concern.

GENERAL CONDITIONS

1. Warranties

It is hereby agreed and warranted that:

1.1 the Insured must pay to the Underwriters all premiums due to the Underwriters;

1.2 the Insured must not notify any claim knowing it to be false or fraudulent as regards amount or otherwise;

1.3 beginning with the Insured's Proposal and continuing to the end of the Period of Insurance the Insured is under a continuing duty to disclose to the Underwriters as soon as is reasonably practicable all material changes, including notice of any extension of underwriting authority.

Any breach of General Condition 1.1, 1.2 or 1.3 above by the Insured will entitle the Underwriters at their discretion to terminate the Policy from the date of inception and all claims shall be forfeited.

2. Claims Conditions Precedent to Liability

The following Conditions are conditions precedent to the Underwriters' liability. No claim will be paid unless full and complete adherence to these Conditions is maintained by the Insured.

2.1 Notification

The Insured shall give notice to the Underwriters as soon as reasonably practicable of:

2.1.1 any Claim made against the Insured and/or

2.1.2 any Circumstance of which the Insured becomes aware during the Period of Insurance.

Provided that such notice as required in 2.1.2 of this Condition has been given during the Period of Insurance any resultant Claim arising from such matters notified, shall be deemed to have been made during the Period of Insurance, provided however that this deeming provision shall only have effect if the Insured complies within a reasonable time and at their own expense with: -

2.1.3 the Underwriters's standard requirement that the notification should state precisely why a Claim is likely and if so, from whom, and

2.1.4 any reasonable request by the Underwriters for further information in relation to the matters notified and

2.1.5 any request by the Underwriters for steps to be taken to reduce or avert the said risk.

For the avoidance of doubt, no other Condition of this Policy shall have the effect of limiting the Underwriters's right to refuse to give effect to this deeming provision in the event of a failure by the Insured to comply with a request under 2.1.3, 2.1.4 and 2.1.5 above.

2.2 Co-operation

Following the occurrence of a Loss, Claim or Circumstance, the Insured shall: -

2.2.1 at their own expense give all information and assistance within timescales reasonably required by the Underwriters and

2.2.2 make no admission of liability, arrangement, compromise, offer, promise or payment without the consent of the Underwriters.

2.2.3 as soon as reasonably practicable inform the police of any Theft and take all practicable steps to discover the guilty party and to recover the stolen property.

3. Underwriters' Rights

Following the notification of a Claim or a Circumstance the Underwriters will be entitled: -

3.1 at its discretion, to take over and conduct in the name of the Insured the investigation, defence or settlement of any such matter;

3.2 at any time, to pay to the Insured the amount of the Limit of Indemnity (less the First Amount Payable and any sum already paid or expended during the Period of Insurance) or any lesser amount for which, in the Underwriters' opinion, any Claim or Claims can be settled and shall then cease to have conduct and control of the Claim or proceedings and be under no further liability in respect of such costs, Claim or Claims. The Underwriters shall not be responsible for any loss which the Insured may claim to have sustained by reason of the Underwriters having so acted;

3.3 to be subrogated to all rights of recovery the Insured may have against any party and the Insured shall do nothing to prejudice such rights. It is agreed, however, that the Underwriters shall not exercise such rights against any Employee except in respect of any claim arising out of the dishonesty of such Employee. The Insured shall execute all papers required and shall do everything necessary to secure and preserve such rights, including the execution of such documents necessary to enable the Underwriters effectively to bring suit in the name of the Insured.

4. Alteration and Assignment

No change in, modification of, or assignment of interest under this Policy shall be effective except when made by a written endorsement to this Policy which is signed by an authorised representative of the Underwriters.

5. Fraud

If any Insured shall make any request for payment in respect of any Loss knowing the same to be false or fraudulent, as regards amount or otherwise, this Policy shall become void and all benefits in terms of this Policy shall be forfeited but only in respect to the individual Insured Person committing such fraud, if applicable.

6. Action Against the Underwriters

No action shall lie against the Underwriters unless, as a condition precedent thereto, there shall have been full compliance with all the terms of this Policy. No persons or organisation shall have any right under this Policy to join the Underwriters as a party to any action against Insureds to determine Insureds' liability nor shall the Underwriters be impeded by the Insureds or their legal representatives. Liquidation or insolvency of an Insured or of the estate of any Insured shall not relieve the Underwriters of his obligations nor deprive the Underwriters of their rights or defences under this Policy.

7. Administrative Conditions - Policy Disputes

Any dispute or difference between the Insured and the Underwriters arising from this Policy shall be referred to Senior Counsel whose identity shall be mutually agreed upon between the Underwriters and the Insured or to any other party as may be mutually agreed.

The findings of the appointed Senior Counsel (or the party as may be mutually agreed) shall be binding upon the Underwriters and the Insured and the costs of such an exercise shall be allocated by the Senior Counsel (or the party as may be mutually agreed) on the basis he/she considers fair and equitable.

8. Prevention of Loss

The Insured shall take all reasonable steps and precautions to prevent Losses/Claims.

9. Other Insurance

If any Loss arising from any claim is Insured by another valid and collectible policy or policies, then this Policy shall apply only in excess of the amount of any deductibles, retentions and limits of liability under such other policy or policies, whether such other policy or policies are stated to be primary, contributory, excess, contingent or otherwise, unless such other insurance is written specifically excess of this Policy by reference in such other policy to this Policy's Policy Number.

10. Take Over and Merger

In the event of a Take-over or Merger any coverage hereunder with respect to Loss shall apply only to an Unfair Labour Practice or Wrongful Act committed or breach of Professional duty or Loss due to a Defined Event insured in terms of the Fidelity Guarantee Section occurring prior to the date of such Take-Over or Merger.

11. Cancellation of Policy

The Insured may cancel this insurance at any time by giving immediate notice to the Underwriters. The Underwriters may cancel this Policy for non-payment of premium by sending not less than ten (10) days notice to the Insured at their last known address. The Underwriters may cancel this Policy under any other circumstances by giving 30 days notice to the Insured in which event the Insured will be entitled to a pro rata return of premium. In the event of the Insured cancelling this Policy, the Underwriters shall retain the customary short rate premium. Payment of any unearned premium by the Underwriters shall not be a condition precedent to the effectiveness of cancellation but such payment shall be made as soon as practicable.

12. Waiver of Right to Cancel

In the event of the Underwriters being entitled to avoid this Policy *ab initio* the Underwriters may at its election instead give notice in writing to the Insured Persons and the Company that they regard this Policy as of full force and effect save that there shall be excluded from any payment afforded hereunder any Loss which has arisen or

which may arise and which is related to the circumstances which entitle the Underwriters to avoid this Policy. This Policy shall then continue in full force and effect but shall be deemed to exclude the particular Loss referred to in the said notice (as if the same had been specifically endorsed *ab initio*).

GENERAL PROVISIONS

1. Aggregate Limit of Indemnity Clause

The maximum amount payable by the Underwriters in respect of all the covers provided by this Policy in respect of any one Loss or Claim and in the aggregate in any one Period of Insurance shall not exceed the Limit of Indemnity stated in the Schedule.

If the Limit of Indemnity or First Amount Payable shall be increased at any time subsequent to inception of the Period of Insurance such increased amount shall apply only to insured events committed / occurring after the date of such increase.

Renewal of this insurance from period to period or any extension of any Period of Insurance shall not have the effect of accumulating or increasing the liability of the Underwriters beyond the Limit of Indemnity stated in the Schedule

For the avoidance of doubt it should be noted that the indemnity afforded under the terms of this Policy is provided jointly to all parties constituting the Insured and for all purposes this Policy shall be considered as a joint policy with one Limit of Indemnity.

2. Automatic Reinstatement of Limit of Indemnity *(Applicable only if stated in the Schedule to be included)*

The payment by the Underwriters of any Loss shall not reduce the Underwriters's liability in respect of any Loss involving dishonesty of other Employees or Claims or Losses arising from unrelated Circumstances provided that the maximum amount payable by the Underwriters for all Losses shall not exceed double the Limit of Indemnity shown in the Schedule in any Period of Insurance.

The maximum amount payable by the Underwriters in respect of all covers provided by the Policy in respect of any one Loss or Claim and in the aggregate in any one Period of Insurance shall not exceed the Limit of Indemnity stated in the Schedule.

3. First Amount Payable

The Insured shall be responsible for the First Amount Payable stated in the Schedule of all Loss / Claims arising from any one Circumstance / Wrongful Act. All Claims arising out of the same Wrongful Act and all interrelated Wrongful acts of the Insured Persons shall be deemed one Claim, and such Claim shall be deemed to be first made on the date the earliest of such Claims is first made against them.

No First Amount Payable shall be payable in respect of Claims under Insuring Agreement A of the Directors' and Officers' Liability section. If Loss arising from a single Claim is covered in part under Insuring Agreement A and in part under Insuring Agreement B, the applicable First Amount Payable set forth in the Schedule shall be applied to that part of the Loss covered by Insuring Agreement B.

4. Territory and Valuation

All premiums, limits, First Amounts Payable, Loss and other amounts under this Policy are expressed and payable in the currency of the Republic of South Africa. If judgement is rendered, settlement is denominated or another element of Loss under this Policy is stated in a currency other than South Africa Rands, payment under this Policy shall be made in South African Rands at the First National Bank (South Africa) selling price rate of exchange as published in Business Day on the date the final judgment is reached or the amount of the settlement is agreed upon or the other element of Loss is due. Cover under this Policy shall extend to insured Circumstances occurring or Claims made worldwide.

5. Representations and Severability

The Insureds agree that in the event that the particulars and statements contained in the Proposal are untrue, this Policy shall not afford any coverage with respect to any of the following Insured:

5.1 any Insured Person who knew at the inception date of this Section of the Policy that the facts concerning himself / herself were not truthfully disclosed in the Proposal;

5.2 the named Insured, if a director or any executive officer knew as of the inception date of this Policy that the facts were not truthfully disclosed in the Proposal.

No fact pertaining to or knowledge possessed by any Insured Person shall be imputed to any other Insured Person for purposes of applying the exceptions set forth in this Policy.

6. Acquisition of the Named Insured

If during the Period of Insurance

6.1the named Insured merges into or consolidates with another organisation, or

6.2another organisation, or persons or group of organisations and/or persons acting in concert acquires securities or voting rights which result in ownership or voting control by the other organisation(s) or persons(s) of more than fifty percent (50%) of the outstanding securities representing the present right to vote for the election of directors of the Insured,

coverage under this Policy shall terminate with immediate effect except in respect of insured Circumstances taking place prior to such merger, consolidation or acquisition.

7. Communication

Wherever this Policy provides that notice be given to the Underwriters, such notice shall be given to:

SECTION 1 – PROFESSIONAL INDEMNITY

INSURING AGREEMENT

The Underwriters agrees to indemnify the Insured:

1. Legal Liability

in respect of Claims made against the Insured and notified to the Underwriters during the Period of Insurance for liability incurred in the conduct of the Insured's Professional Business as a result of breach of professional duty arising out of negligence on the part of:

1.1 the Insured

1.2 any Employee.

2. Loss of Documents

against any reasonable cost or expense incurred by the Insured to which the Underwriters have consented (which consent shall not be unreasonably withheld) in replacing and restoring Documents either owned by, or which are the responsibility of the Insured in the conduct of the Insured's Professional Business, which are discovered to be lost or damaged and notified to the Underwriters during the Period of Insurance.

DEFINITIONS AND INTERPRETATIONS

For the purposes of this Section

Documents mean:

all forms of documents of whatsoever nature including computer system records (provided the Insured maintains duplicates of computer system records).

Employee means:

any person currently (or who at the time of the Circumstance was) employed under a contract of service with the Insured including partners, executive and non executive directors, consultants and temporary employees employed by the Insured.

Firm means:

1. the Firm(s) identified as the Insured in the Schedule and named in the Proposal being either a partnership comprised solely of the partners and former partners, sole trader or corporate body;

2. any firm(s) or business(es) or any subsidiary firm(s) or subsidiary business(es) for which the Insured is legally liable in consequence of their acquisition (whether partial or otherwise) either prior to the inception of this Policy or during the Period of Insurance provided the Underwriters have been notified in writing of their existence and have agreed to insure such firm(s) or business(es).

Insured means

1. the Firm;

2. any partner, director or principal of the Firm including any person appointed to such position during the Period of Insurance;

3. any former partner, director or principal of the Firm;

4. the estate, personal representatives or trustee or assignee in the event of the insolvency of 1, 2 and / or 3 but

only in regard to liability incurred by those described above.

SPECIFIC EXCLUSIONS

This Section of the Policy shall not indemnify the Insured in respect of any Claim, Loss, liability or expense arising directly or indirectly out of:

1. Activities as Agent

any claim or loss by any insurer or underwriter by reason of any negligent act, error or omission committed in the course of the Insured's activities as agent of such insurer or as claims adjusters.

2. Bodily Injury and Property Damage

2.1 any bodily, mental or emotional injury, sickness, disease or death, or

2.2 any loss of or damage to property, other than covered under Insuring Agreement 2

of any third party unless such Claim, loss, liability or expense arises from negligent advice.

3. Breach of Contract of Employment

any contract of service or obligation owed by the Insured as employer including any Claim for wrongful or unfair dismissal.

4. Computer Network and Data Corruption

4.1 the corruption, erasure, theft, alteration of, or

4.2 the access or lack of access to, or

4.3 the interference with

electronically held data of or held by the Insured wholly or partly caused by any computer virus or by any person not being a partner, director or employee currently employed by the Insured.

5. Computer Records

loss, distortion or erasure of computer records

5.1 whilst mounted in or on any machine for use or processing unless caused by any negligent act or omission on the part of the Insured or

5.2 resulting from wear, tear, vermin or gradual deterioration or

5.3 caused by climatic or atmospheric conditions or extremes of temperature or

5.4 due to the presence of magnetic flux or due to loss of magnetism.

6. Controlling Interest / Associated Companies

any Claim by

6.1 any parent or subsidiary company of the Insured or any company having the same parent company as the Insured or

6.2 any other company in which the Insured has a shareholding in excess of 50% or

6.3 any other company in common ownership with the Insured

unless such Claim emanates from an independent third party.

7. Dishonesty

the dishonesty of the Insured or any Employee.

8. Employers' Liability

bodily injury, sickness, disease or death sustained by any person arising out of and in the course of their employment by the Insured in any capacity.

9. Geographical and Jurisdiction Limits

9.1 work in connection with any contract performed outside the Geographical Limits or

9.2 any judgment, award, payment or settlement made within countries which operate under the laws of the United States of America or Canada or

9.3 any order made anywhere in the World to enforce any judgement, award or settlement either in whole or in part, made in the courts of or under the laws of the United States of America or Canada.

10. Insolvency

or from the insolvency, curatorship, bankruptcy, liquidation or financial inability to pay, of the Insured or any insurance company, reinsurance company, underwriter, syndicate, agent, broker or intermediary, benefit plan, self insurance plan, insurance pool or risk retention group, financial institution or other risk bearing entity with whom, or through whom, coverage has been placed or obtained.

11. Financial Guarantee

financial default, bankruptcy or insolvency of any party or person, whether a party to this contract or not, other than in respect of Claim(s) arising from any negligent act, error or omission committed or alleged to have been committed by the Insured.

For the purposes of this Exclusion the term “negligent act, error or omission” shall include but not be limited to misstatement, misleading statement, breach of duty, breach of trust, breach of warranty of authority.

12. Defamation or Breach of Confidentiality

defamation or breach of confidentiality committed or allegedly committed by any person.

13. Other Insurance

a situation where the Insured is entitled to indemnity under any other insurance except in respect of any sum beyond the amount which would have been payable under such other insurance had this Section of the Policy not been effected.

14. Suitability of Insurers

breach of the Insured’s duty to advise on the suitability (which expression shall, without prejudice to the generality of such term, include financial standing) of any insurance company, insurer or underwriter with whom insurance or reinsurance is placed.

15. Warranty or Guarantee

the giving by the Insured of any warranty, indemnity or guarantee or financial obligation assumed by the Insured under contract unless such liability would have attached to the Insured notwithstanding such express agreement.

16. Disclosure of Commission

a dispute concerning the payment of commission, fees or other remuneration to the Insured.

17. Failure to Account for Monies

failure on the part of the Insured to account for money.

18. Market Fluctuation

the depreciation or loss of investments when such depreciation or loss is a result of normal or abnormal fluctuations in any financial stock or commodity or other markets which are outside the control of the Insured.

AUTOMATIC EXTENSIONS TO SECTION 1

1. Breach of Confidentiality Extension

Notwithstanding Specific Exclusion 11, this Section is hereby extended to indemnify the Insured in respect of any Claim or Claims made against the Insured and notified to the Underwriters during the Period of Insurance incurred in the conduct of the Insured's Professional Business as a result of any unintentional breach of confidentiality. Provided that the liability of the Underwriters shall not exceed in respect of any one Claim and in the aggregate in the Period of Insurance the sub-limit stated in the Schedule.

2. Defamation Extension

Notwithstanding Specific Exclusion 11, this Section of the Policy is hereby extended to indemnify the Insured in respect of Claims made against the Insured and notified to the Underwriters during the Period of Insurance incurred in the conduct of the Insured's Professional Business as a result of defamation committed without intentional malice by the Insured or any Employee. Provided that the liability of the Underwriters shall not exceed in respect of any one Claim and in the aggregate in the Period of Insurance the sub-limit stated in the Schedule.

OPTIONAL EXTENSIONS TO SECTION 1

1. Employee Dishonesty Extension *(Applicable only if so stated in the Schedule)*

Notwithstanding anything contained in the Policy to the contrary, the Underwriters agree to indemnify the Insured in respect of Claims made against the Insured and notified to the Underwriters during the Period of Insurance incurred in the conduct of the Insured's Professional Business as a result of any dishonest or fraudulent act or omission on the part of any Employee.

Provided that

1. no person committing or condoning such dishonest or fraudulent act or omission shall be entitled to indemnity;

2. no indemnity shall be provided for dishonest or fraudulent acts committed by any person after discovery by the Insured or reasonable cause for suspicion of fraud or dishonesty on the part of that person;

3. no indemnity shall be provided for dishonest or fraudulent acts committed by any partner or director of the Insured;

4. the Insured takes all reasonable steps to effect recovery from any person committing or condoning any dishonest or fraudulent act or omission or from the estate and/or legal representatives of such person;

5. the following shall be deducted from any amount payable by the Underwriters

5.1 any monies which, but for such dishonest or fraudulent act or omission, would be due from the Insured to the person committing or condoning such act or omission,

5.2 any monies held by the Insured and belonging to such person,

5.3 any monies recovered following action described in 4 above,

to the extent that the Insured is legally permitted to withhold such money.

2. Underwriting and/or Claims Mandate Authority Extension *(Applicable only if so stated in the Schedule)*

Notwithstanding anything contained in the Policy to the contrary, the Underwriters agree to indemnify the Insured in respect of Claims made against the Insured and notified to the Underwriters during the Period of Insurance incurred in the conduct of the Insured's Professional Business as a result of breach of professional duty arising out of negligence in respect of the operation of Underwriting and/or Claims Mandate Authorities issued or granted to the Insured.

Provided that this Extension shall not indemnify the Insured in respect of any claim or claims, loss. Liability or expense arising directly or indirectly out of underwriting or trading losses under the Underwriting Authorities operated by the Insured unless such claim or claims arise(s) from the unintentional breach of any granted Underwriting Authority and/or Claims Mandate Authorities.

SECTION 2 – DIRECTORS AND OFFICERS LIABILITY

INSURING AGREEMENTS

A - Directors and Officers Individual Cover

The Underwriters shall pay on behalf of the Insured Persons Loss for which the Insured Persons are not indemnified by the Company and for which the Insured Persons become legally obligated to pay on account of any claim first made against them, individually or otherwise, during the Period of Insurance for a Wrongful Act taking place on or after the Retroactive Date shown in the Schedule and prior to the expiry of the Period of Insurance.

B - Company Reimbursement Cover

The Underwriters shall reimburse the Company for Loss arising from the Company's indemnification of the Insured Persons, as permitted or required by law, and for which the Insured Persons have become legally obligated to pay on account of any claim first made against them, individually or otherwise, during the Period of Insurance for a Wrongful Act taking place on or after the Retroactive Date shown in the Schedule and prior to the expiry of the Period of Insurance.

SPECIFIC EXTENSIONS

1. Estates and Legal Representatives

This Section shall afford cover for Claims for the Wrongful Acts of Insured Persons made against the estates, heirs, legal representatives or assigns of Insured Persons who are deceased or against the legal representatives or assigns of Insured Persons who are incompetent, insolvent or liquidated to the extent that, in the absence of such death, incompetence, insolvency or liquidation, such claims would have been covered under this Section of the Policy.

2. Spousal Liability

If a Claim against an Insured Person includes a Claim against the Insured Person's lawful spouse solely by reason of

2.1 such spouse's legal status as a spouse of the Insured Person, or

2.2 such spouse's ownership interest in property which the claimant seeks as recovery for alleged Wrongful Acts of the Insured Person,

all Loss which such spouse becomes legally obligated to pay by reason of such Claim shall be treated for purposes of this Section of the Policy as Loss which the Insured Person becomes legally obligated to pay on account of the Claim made against the Insured Person. All terms and Conditions of this Policy, including without limitation the First Amount Payable, applicable to Loss incurred by such Insured Person in the Claim shall also apply to such spousal Loss.

The cover afforded by this extension does not apply to the extent that the Claim alleges any Wrongful Act or omission by the Insured Person's spouse.

SPECIFIC DEFINITIONS

For the purposes of this Section

Claim means:

1. a written demand;

2. a civil proceeding including third party proceeding, counterclaim or arbitration proceeding commenced by the service of a writ, summons or similar proceeding;

3. a criminal proceeding against any Insured Person(s) commenced by a return of an indictment or similar process;

4. a formal administrative or regulatory proceeding commenced by the filing of a notice of charges, formal investigative order or similar document;

5. an arbitration proceeding for a Wrongful Act, including any appeal therefrom.

Company means:

the organisation(s) named in the Schedule as Insured and its/their subsidiaries.

Financial Impairment means:

the status of the Company resulting from either the appointment by any governmental official, agency or court of a liquidator, trustee, curator or similar official to take control of, supervise, manage or liquidate the Company or the Company becoming a debtor in possession.

Insured means:

the Insured Persons and, solely in respect of Insuring Agreement B , the Company.

Insured Person means:

1. any one or more persons who were, now are or shall be duly elected or appointed directors or Officers of the Company; and

2. any one or more other natural persons not described in subparagraph 1 above who were, now are or shall be full or part-time employees of the Company, provided that the Claim is initially made against both such natural persons and one or more Insured Persons described in subparagraph 1 above; and

Insured Persons shall not include external auditors appointed by the Company

Interrelated Wrongful Acts means:

all Wrongful Acts that have as a common nexus any fact, Circumstances, situations, events, transaction, cause or series of related facts, Circumstances, situations, events, transactions or causes.

Loss means:

the amount which the Insured Persons or, the Company becomes legally obligated to pay on account of each Claim and for all Claims in the Period of Insurance made against them for Wrongful Acts for which cover applies, including, but not limited to, damages, judgments, settlements and Defence Costs including adverse court cost orders or Underwriters sanctioned agreement to pay legal costs.

Loss does not include

1. any amount for which the Insureds are absolved from payment;

2. taxes, fines or penalties imposed by law;

3. the multiple portion of any multiplied damage award or punitive or exemplary damages incurred by Insured Persons; or

4. matters uninsurable under the law pursuant to which this Policy is construed;

provided this definition does not exclude punitive or exemplary damages incurred by the Insured to the extent such damages are insurable under applicable law.

Officer means:

anyone who occupies an executive, managerial or supervisory position within the Insured Company.

Parent Company means:

the organisation named as the Insured in the Schedule.

Security(ies) means:

any shares in the capital of a company and includes stock and debentures convertible into shares and any rights or interests in a company or in respect of any such shares, stock or debentures.

Wrongful Act means:

1. any error, misstatement, misleading statement, act, omission, negligence, or breach of duty actually or allegedly committed or attempted by any of the Insured Persons, individually or otherwise, in their capacity as such, or

2. any matter claimed against the Insured Persons solely by reason of their serving in such capacity.

Except as may be otherwise specifically provided in this Section of the Policy, Wrongful Act does not include any conduct actually or allegedly committed or attempted by Insured Persons in their capacity as a director, officer, trustee or employee of any organisation other than the Company, even if service in such capacity is with the knowledge and consent of, at the direction or request of, or part of the duties regularly assigned to the Insured Persons by the Company.

SPECIFIC EXCLUSIONS

The Underwriters shall not be liable for Loss on account of any Claim

1. based upon, arising out of, or attributable to any fact, Circumstance or situation which has been the subject of any written notice given under any policy of which this Policy is a renewal or replacement;

2. based upon, arising out of, or attributable to any prior or pending litigation against the Company or any Insured Persons as of the applicable prior litigation date, if any, set forth in the Schedule or the same or substantially the same fact, Circumstance or situation underlying or alleged therein;

3. brought or maintained by or on behalf of the Company or any Insured Persons in any capacity except:

    3.1 a Claim that is brought or maintained on behalf of the Company by one or more persons who are not Insured Persons and who bring and maintain the Claim without the solicitation or instigation of the Company or any Insured Persons,

    3.2 a Claim brought or maintained by any Insured Persons for contribution or indemnity, if the Claim directly results from another Claim covered under this Section of the Policy, or

    3.3 a Claim brought or maintained by any employee of the Company described in the definition of Insured Persons sub-paragraph 2.

4. based upon, arising out of, directly or indirectly resulting from, in consequence of or in any way involving any retirement fund, profit sharing or employee benefit or Company welfare programme or any share option, share incentive scheme or trust established in whole or in part for the benefit of any of the directors, Officers or employees of the Company;

6. for bodily injury, mental anguish, emotional distress, sickness, disease or death of any persons, or for damage to or

destruction of any tangible property including loss of use thereof, or for defamation of character or violation of a person's right of privacy

7. arising from any Wrongful Act which occurred prior to the Retroactive Date (if any) stated in the Schedule provided that nothing contained within this exclusion shall be interpreted as releasing the Insureds from their obligation to disclose, as a material fact, all details of Claims made or outstanding or events likely to give rise to a Claim;

8. in respect of United States of America exposures:

   8.1 companies or subsidiaries with shares listed on a stock exchange located in the United States of America; or

   8.2 punitive, exemplary or aggravated damages; or

   8.3 any Claim arising out of or involving American depository receipts; or

   8.4 prospectus liability; or

   8.5 arising from or involving the laws or regulations or supervisory powers of the Securities and Exchange Commission of the United States of America;

9. for any fraudulent act or omission or any willful violation of any statute or regulation if a judgment or other final adjudication adverse to such Insured establishes that such Insured committed, in fact, such an act, omission or willful violation; or

10. based upon, arising out of, or attributable to such Insured gaining, in fact, any personal profit, remuneration or financial advantage to which such Insured Person was not legally entitled.

11. based upon, arising from or in consequence of the rendering or failure to render professional services.

12. based upon, arising from or in consequence of the failure to arrange, maintain or buy insurance.

SPECIFIC CONDITIONS AND LIMITATIONS

1. Indemnification

If the Company is permitted or required by common or statutory law, but fails or refuses, other than for reason of financial impairment, to advance Defence Costs or indemnify the Insured Persons for Loss, then, notwithstanding any other conditions, provisions or terms of this Policy to the contrary, any payment by the Underwriters of such Defence Costs or other Loss shall be subject to

1.1 the First Amount Payable set forth in the Schedule, if any, and

1.2 all of the Exclusions set forth in this Policy.

For purposes of this Specific Condition, the shareholder and board of director resolutions of the Company shall be deemed to provide indemnification for such Defence Costs or other Loss to the fullest extent permitted by law.

2. Defence and Settlement

Subject to the provisions of this clause it shall be the duty of the Insureds and not the duty of the Underwriters to defend any Claim.

The Insureds agree not to settle or offer to settle any Claim, incur any Defence Costs or otherwise assume any contractual obligation or admit any liability with respect to any Claim without the Underwriters' written consent. The Underwriters shall not be liable for any settlement, Defence Costs, assumed obligation or admission to which it has not consented. In respect of any Claim submitted for cover under this Section of the Policy, the Underwriters shall have the

right and shall be given the opportunity to effectively associate with, and shall be consulted in advance by, the Insureds regarding

2.1 the selection of appropriate defence attorneys and counsel,

2.2 substantive defence strategies including, without limitation, decisions regarding the filing and content of substantive motions, and

2.3 settlement negotiations.

The Insureds agree to provide the Underwriters with all information, assistance and co-operation which the Underwriters reasonably requests and agree that in the event of a Claim the Insured will do nothing that shall prejudice the Underwriters' position or their potential or actual rights of recovery. The Underwriters may make any investigation they deems necessary.

The Underwriters may, with the written consent of the Insured, settle any Claim for solely a monetary amount, which the Underwriters deem reasonable. If the Insured withholds consent of such settlement, the Underwriters' liability for all Loss on account of such Claim shall not exceed the amount for which the Underwriters could have settled such Claim plus Defence Costs accrued as at the date such settlement was proposed in writing by the Underwriters to the Insured.

The Underwriters and the Insureds shall not unreasonably withhold any consent referenced in this condition.

3. Advancement of Costs

Subject to Specific Condition 4, Allocation below, the Underwriters shall advance on behalf of the Insureds Defence Costs which the Insured Persons, or the Company, have incurred in connection with Claims made against them, prior to disposition of such Claims, provided that to the extent it is finally established that any such Defence Costs are not covered under this Policy, the Insureds, severally according to their interests, agree to repay the Underwriters such Defence Costs.

4. Allocation

If, in any Claim, the Insured incur Loss jointly with others, including the Company with respect to any Claim, or incur an amount consisting of both Losses covered by this Section of the Policy and loss not covered by this Section of the Policy because the Claim includes both covered and uncovered matters, then the Insureds and the Underwriters shall allocate such amount between covered Loss and uncovered loss based upon the relative legal exposures of the parties to covered and uncovered matters.

If there is agreement on the allocation of Defence Costs, the Underwriters shall advance on a current basis Defence Costs allocated to the covered Loss. If there is no agreement on the allocation of Defence Costs, the Underwriters shall advance on a current basis Defence Costs which the Underwriters believes to be covered under this Section of the Policy until a different allocation is negotiated, arbitrated or judicially determined. Any advancement of Defence Costs shall be subject to, and conditional upon, receipt by the Underwriters of a written undertaking by the Insureds that such advanced amounts shall be repaid to the Underwriters by the Insureds severally according to their respective interests if and to the extent the Insureds shall not be entitled under the terms and Conditions of this Policy to cover for such Defence Costs.

Any negotiated, arbitrated or judicially determined allocation of Defence Costs on account of a Claim shall be applied retroactively to all Defence Costs on account of such Claim, notwithstanding any prior advancement to the contrary. Any allocation or advancement of Defence Costs on account of a Claim shall not apply to or create any presumption in respect of the allocation of other Loss on account of such Claim or any other Claim.

5. Changes in Exposure

5.1 Acquisition or Creation of Another Organisation

If during the Period of Insurance the Company

5.1.1 acquires securities in another organisation or creates another organisation, which as a result of such acquisition or creation becomes a Subsidiary, or

5.1.2 acquires any organisation by merger into or consolidation with the Company,

such organisation and its qualifying directors and Officers shall be covered under this Policy as follows:

a) If the fair value of all cash, securities, assumed indebtedness and other consideration paid by the Company for any such acquisition or creation is less than 10% of the total assets of all of the companies as reflected in the Company's most recent financial statements as at the inception of the Period of Insurance, such organisation and its directors, Officers and qualifying employees shall automatically be covered under this Section of the Policy, but only with respect to Wrongful Acts taking place after such acquisition or creation, unless the Underwriters agree after presentation of the complete application and all appropriate information to provide cover by endorsement for Wrongful Acts taking place prior to such acquisition or creation.

b) In respect of all other acquisitions or creations described in 5.1.1 and 5.1.2 above, such organisation and its directors, Officers and qualifying employees shall automatically be covered under this Section of the Policy but only for ninety (90) days or the remainder of the Period of Insurance, whichever is less, following the effective date of such acquisition or creation ("Automatic Cover Period") and only in respect of Wrongful Acts taking place after such acquisition or creation. The Parent Company, as a condition precedent to further cover in respect of such organisation and persons after such Automatic Cover Period, shall give written notice of such acquisition or creation to the Underwriters as soon as reasonably possible but in no event later than forty-five (45) days following the effective date of such acquisition or creation, and shall thereafter promptly provide to the Underwriters such information as the Underwriters may request.

Upon receipt of such notice and other information, the Underwriters shall promptly provide to the Parent Company a quotation for cover under this Section of the Policy for such organisation and persons for the remainder of the Period of Insurance. If the Parent Company fails to comply with such condition precedent, or if within thirty (30) days following receipt of such quotation the Parent Company fails to pay any additional premium or fails to agree to any additional cover terms and conditions as set forth in such quotation, cover otherwise afforded by this clause for such organisation and persons shall terminate upon expiration of such Automatic Cover Period.

5.2 Cessation of Subsidiaries

If before or during the Period of Insurance an organisation ceases to be a Subsidiary, cover in respect of such Subsidiary and its Insured Persons shall continue until termination of this Section of the Policy but only in respect of Claims for Wrongful Acts taking place prior to the date such organisation ceased to be a Subsidiary.

SECTION 3 – EMPLOYMENT PRACTICES LIABILITY

INSURING AGREEMENT

The Underwriters agree to indemnify the Insured for Loss arising from any Claim first made during the Period of Insurance and reported to the Underwriters in accordance with the terms, conditions, provisions and exclusions of the Policy, for any actual or alleged Unfair Labour Practice committed or alleged to have been committed on or after the Retroactive Date stated in the Schedule.

SPECIFIC DEFINITIONS

For the purposes of this Section

Claim means:

1. any legal, administrative or regulatory proceeding, including the issue of a writ or summons or cross-claim or counter-claim issued or initiated against or served upon the Insured; or

2. any written allegation of an Unfair Labour Practice communicated to the Insured and evidencing an intention to hold the Insured responsible.

More than one Claim arising out of the same Unfair Labour Practice shall be deemed to constitute a single Claim first made at the time that the earliest such Claim was first reported.

The term Claim shall not include any labour or grievance proceeding pursuant to a collective bargaining agreement.

This insurance shall apply to such Claims made anywhere in the world.

Company means:

the company named in the Schedule as the Insured and its Subsidiary Companies.

Employee means:

1. any Independent Contractor to the Company, but only to the extent that the Company agrees in writing in advance of any Unfair Labour Practice to indemnify such person. Any such indemnity shall be in addition to any indemnity otherwise available to the Independent Contractor or any affiliate of the Independent Contractor;

2. any person, excluding an Independent Contractor, who works for another person and receives or is entitled to receive any remuneration from the Company;

3. any other person who, in any manner, assists in carrying on or conducting the business of the Company.

Independent Contractor means:

any natural person who is not in the full-time employment of the Company but who renders service to the Company subject to a contract for specified services.

Insured means:

the Company as defined and the Insured persons:

Insured Persons means:

1. any natural person who was at the time of the Unfair Labour Practice a director, officer or Employee of the Company and acting in their capacity as such;

2. the estate, heirs, legal representatives or assigns of any person described in 1 above who dies, becomes insolvent or legally incompetent and has incurred liabilities due to any Unfair Labour Practice;

3. the lawful spouse of any person described in 1 above, but only to the extent that such spouse is a party to a Claim solely in their capacity as lawful spouse of the aforesaid person, and only for the purpose of any Claim seeking damages which are recoverable from marital community property, property jointly held by the aforesaid person and the lawful spouse, or property transferred from the aforesaid person to the lawful spouse, and only to the extent that the aforesaid person is entitled to indemnity for such Claim.

Loss means:

1. damages, judgments and costs awarded against the Insured by a bargaining council, the Commission for Conciliation Mediation and Arbitration (CCMA), the Labour Court or the Labour Appeal Court;

2. settlements entered into with the Underwriters' prior written consent, which will not be withheld unreasonably;

3. Defence Costs as defined herein.

Loss shall not include

1. taxes, levies, fines, penalties, punitive, exemplary, aggravated or multiplied damages or any claim uninsurable by law, except for exemplary or aggravated damages if awarded by the CCMA or Labour Court in connection with a Claim for unfair dismissal or arising from any Claim for defamation;

2. any obligation arising from any law or regulation in any jurisdiction in respect of workers' compensation, disability benefits, redundancy or unemployment benefits or compensation, unemployment insurance, retirement benefits, social security benefits or compensation, or any similar law or regulation;

3. any employment related benefits, stock options, deferred compensation, changing of Company Policy, affirmative action, education/sensitivity training or any other type of compensation other than salaries, bonuses and wages;

Period of Insurance means:

the Period of Insurance stated in the Schedule; except that in the event of the take-over or merger of the Company, the Period of Insurance shall mean the Period of Insurance plus 180 days thereafter.

Notwithstanding any other provision of this Policy, the Period of Insurance shall not exceed a period of eighteen (18) calendar months from the earliest date stated in the Schedule.

The limit of the Underwriters's aggregate liability shall not be increased by any provision of this Policy as to the Period of Insurance.

Service Provider means:

the employers' organization or labour professional named in the Schedule who is authorised to represent the Insured at the CCMA or Labour Court.

Unfair Labour Practice means:

1. unfair discrimination against any Employee in any employment policy or practice on any one or more grounds of race, gender, sex, pregnancy, ethnic or social origin, colour, sexual orientation, age, disability, religion, HIV status, conscience, belief, political opinion, culture, language, marital status or family responsibility;

2. sexual harassment including unwelcome sexual advances, requests for sexual favours and any unwelcome verbal, visual or physical contact of a sexual nature which

    2.1 is explicitly or implicitly made a condition or term of employment;

2.2 creates a hostile or offensive working environment;

2.3 when rejected or opposed by a person becomes a basis for decisions regarding the person's employment;

3. defamation which relates to a person's job skills, job performance, qualifications for employment, professional reputation, disciplinary history or termination of employment;

4. unfair dismissal, discharge or termination of employment or refusal to hire any prospective Employee;

5. adverse change in the terms and conditions of a person's employment in retaliation for that person's exercise of his or her rights under law, or support of the rights of another.

Related, continuous, repeated or causally connected Unfair Labour Practices shall for the purpose of this Section of the Policy constitute a single Unfair Labour Practice.

SPECIFIC EXTENSION

New Subsidiary

In the event of the creation or acquisition of a Subsidiary Company after the inception date of this Section of the Policy:

a) if, on the date created or acquired the total number of employees of the Subsidiary Company do not exceed 10% of the number of employees of the Company, the Subsidiary Company is automatically covered by the Policy and the Underwriters waive any reporting requirements;

b) if, on the date created or acquired, the total number of employees of the Subsidiary Company is greater than 10% of the number of employees of the Company, the Subsidiary shall be deemed a Subsidiary hereunder upon written notice thereof being given to the Underwriters within 90 days thereafter and the Underwriters agreeing to extend coverage, subject to receipt of such information as the Underwriters may request and payment of any additional premium required.

Provided, however, that automatic coverage provided per a) and b) above shall apply only in respect of an Unfair Labour Practice committed or alleged to have been committed by any Insured subsequent to the date of such acquisition or creation.

SPECIFIC EXCLUSIONS

The Underwriters shall not pay any Loss

1. arising from or in any way involving any actual dishonest, willful, fraudulent or malicious act of the Insured;

2. brought about by, or contributed to by, or consequent upon, any litigation instigated against any Insured which was in existence prior to or pending at the inception of the Policy;

3. arising out of industrial disputes or negotiations, trade union activities or trade union membership except for costs and expenses incurred in obtaining an interdict in the case of an unprotected strike action;

4. for actual or alleged entitlement to insurance or other benefits under any workers' compensation, unemployment compensation, disability, retirement or social security laws, rules and regulations;

5. for Loss other than Defence Costs which constitutes the cost of compliance with any obligation to adapt premises or working methods to the needs of a person with a disability or to meet statutory health and safety standards or similar provisions of any statutory, civil or common law;

6. for breach of any minimum wage regulations, breach of any statutory or procedural duty or requirement in a redundancy, non-payment of statutory maternity or sick pay or similar provisions of any state, local or common law;

7. which constitutes compensation in respect of a notice period, or is determined to be owing under an express written contract of employment or pursuant to an express written obligation to make payments in the event of termination of employment.

For the purpose of determining the applicability of the above exclusions the conduct of an Insured Person or the Company shall not be imputed to any other Insured Person.

SPECIFIC CONDITION

Additional Claims and Notice Provisions

1. The Insured shall, prior to dismissing or taking any other disciplinary action against an employee, contact the service provider named in the Schedule.

   The Insured shall follow any advice or instruction offered by the service provider in respect of such proposed dismissal or disciplinary action, and failure to do so may result in any subsequent claim arising there from being rejected by the Underwriters.

2. Insured Persons or the Company shall not be required to contest any legal proceedings unless Counsel (to be mutually agreed upon by the Insured Persons, the Company and the Underwriters) shall advise that such proceedings ought to be contested having regard to the prospect of success and other relevant circumstances.

3. The Underwriters shall not settle any Claim without the consent of the Insured Persons or the Company. If, however, the Insured Persons or the Company shall refuse to consent to any settlement recommended by the Underwriters and shall elect to contest or continue any legal proceedings in connection with such Claim, then the Underwriters' liability for the Claim shall not exceed the amount by which the Claim could have been so settled inclusive of Defence Costs incurred with their consent up to the date of such refusal, and then only up to the limit of the Underwriters' Liability stated in the Schedule.

4. The Underwriters shall be entitled to nominate an attorney and, if appropriate, an advocate of its choice to represent the Insured Persons and the Company.

SECTION 4 – FIDELITY GUARANTEE

INSURING AGREEMENT

The Underwriters agree to indemnify the Insured in respect of the Defined Events occurring subsequent to the Retroactive Date stated in the Schedule and discovered by the Insured during the Period of Insurance.

DEFINED EVENTS

1 Loss of money and / or other property belonging to the Insured or for which the Insured is responsible stolen by an Employee (as defined hereafter);

2 Direct financial loss sustained by the Insured as a result of fraud or dishonesty of an Employee which results in dishonest personal financial gain for the Employee concerned or his/her nominee;

3. Loss sustained by the Insured directly caused by Theft by Computer Fraud;

4. Direct financial loss due to Electronic Data Loss.

Provided that

1. where indemnity is provided to the Insured in terms of any insurance superseded by this Policy the liability of the Underwriters shall be limited to only that proportion of the loss which is not payable in terms of the superseded policy;

2. all acts committed by any one person or in which such person is involved or implicated will be considered one Occurrence;

3. the term dishonest personal financial gain shall not include gain by an Employee in the form of salary increases, fees, commissions, bonuses, promotions or other emoluments, except when such salary increases, fees, commissions, bonuses, promotions or other emoluments result directly from a specific dishonest act on the part of that Employee.

SPECIFIC DEFINITIONS

For the purposes of this Section

Computer Fraud means:

the unlawful making, with intent to defraud, of a misrepresentation by means of access to or use, disclosure, processing, deletion, insertion, amendment, interception or manipulation of the information, data, software or systems of the Insured or of any banking institution holding, controlling or otherwise dealing with money or property of the Insured or for which the Insured is responsible which is initiated, implemented or completed electronically by use of a computer.

Electronic Data Loss means:

(a) malicious alteration or destruction of electronic data or attempt thereat by any Third Party while such data is lawfully within the Insured's computer system or a service provider's system or while recorded upon electronic data processing media within the offices of the Insured or in the custody of a person designated by the Insured to remove such electronic data processing media from the offices of the Insured provided that the Insured is the true owner of such programs or is legally liable for such loss;

(b) electronic data processing media being lost damaged or destroyed as a direct result of robbery, burglary, theft or malicious act while located as in (a) above;

(c) malicious alteration or destruction of electronic computer programs while lawfully stored within the Insured's computer system provided that the Insured is the true owner of such programs or is legally liable for such alteration or destruction.

Employee means:

1. any person while employed under a contract of service with or apprenticeship to the Insured;

1. any person while hired or seconded from any other party into the service of the Insured whom the Insured has the right at all times to govern control and direct in the performance of work done in the course of the business of the Insured.

Loss means:

the actual loss of money or monetary funds or negotiable instruments or corporeal tangible property belonging to the Insured or for which the Insured is responsible provided that Loss does not include a loss arising from the avoidance, breach, cancellation or other termination of a contract, the non-payment or other non-performance by a debtor, the adverse consequences of a business or trade risk or venture or other speculative enterprise or investment or the provision or receipt of any suretyship or other security.

Theft means:

the dishonest appropriation of money, monetary funds or property with the intention of permanently depriving the owner of such money, monetary funds or property.

Third Party means:

any person other than an Employee or director of or principal, partner or member in the Insured.

SPECIFIC EXCLUSIONS

1. The Underwriters shall not be liable for

    1.1 Loss resulting from or contributed to by any Defined Event by

        1.1.1 any partner in or of the Insured or by any principal, director or member of the Insured unless such partner, principal director or member acts in an executive capacity or such principal, director or member is also an Employee;

        1.1.2 any Employee or partner from the time the Insured becomes aware that such Employee or partner has committed any fraud or dishonesty;

    1.2 any consequential or other indirect losses of any kind following Losses referred to under any Defined Events.

2. The Policy does not cover any company or other legal entity acquired by the Insured during the currency of the Policy unless endorsed on the Policy.

3. If the Insured is a company, close corporation or partnership and any principal, shareholder, director, member or partner thereof is involved or implicated in the Loss the Underwriters shall only be liable to the extent of the shareholding, participation, membership or other share of the other principals, shareholders, directors, members or partners of the Insured.

4. In respect of Defined Events 1 and 2 the Underwriters shall not be liable for any loss for which indemnity is provided in terms of a Money Insurance Policy held by the Insured except in respect of any amount in excess of the indemnity provided by such policy.

5. In respect of Defined Event 3 the Underwriters shall not be liable for any Loss which is insured or which would be insurable in terms of a Money or Theft Insurance Policy.

SPECIFIC CONDITIONS

1. Maintenance of Systems and Procedures

The Insured shall institute and/or maintain and continue to employ in every material manner all such systems of check and control, accounting and clerical procedures and methods of conducting his business as has been represented to the Underwriters by the Insured but the Insured may

1.1 change the remuneration and conditions of service of any Employee

1.2 make any other changes as are approved beforehand in writing by the Insured's auditors.

2. Apportionment of Recoveries

If the Insured shall sustain any Loss which exceeds the Limit of Indemnity hereunder in respect of such Loss the Insured shall be entitled to all recoveries (except from suretyship, insurance, reinsurance, security or indemnity taken or effected by the Underwriters or for the amount of any deductible / First Amount Payable) by whomsoever made on account of such Loss until fully reimbursed less the actual cost of effecting the same and any remainder shall be applied to the reimbursement of the Underwriters.

3. Claims

3.1 In the event of a claim being rejected and legal action not being commenced within 12 (twelve) months after such rejection all benefit afforded under the Policy in respect of any such claim shall be forfeited.

3.2 If, after the payment of a claim in terms of this Section of the Policy, the property (the subject matter of the claim) or any part thereof is located the Insured shall render all assistance in the identification and physical recovery of such property, if called upon to do so by the Underwriters, provided that the Insured's reasonable expenses in rendering such assistance shall be reimbursed by the Underwriters. Should the Insured fail to render assistance in terms of this condition when called upon to do so, the Insured shall immediately become liable to repay to the Underwriters all amounts paid in respect of the claim.

3.3 Where amounts recoverable from the Underwriters are delayed pending finalisation of any claim, payments on account may be made to the Insured, if required, at the discretion of the Underwriters.

4. Other Insurances

It is a condition precedent to the liability of the Underwriters that other than

4.1 a Money policy,

4.2 a policy declared to the Underwriters at inception or renewal of this policy or at the time a claim is submitted,

4.3 a pension fund trustees Fidelity Insurance policy,

4.4 this Policy,

no other policy is in force or will be effected during the currency of this Policy to insure against the risks insured hereunder, but should a policy referred to in 4.2 be declared, the Underwriters of this Policy shall be liable to make good only a rateable proportion of the amount payable to the Insured in the event of a claim.

CLAUSES AND EXTENSIONS

1. Claims Preparation Costs

The insurance under this Policy is extended to include costs reasonably incurred by the Insured in producing and certifying any particulars or details required by the Underwriters in terms of General Condition 2 or to substantiate the amount of any claim, provided that the liability of the Underwriters for such costs shall not exceed in respect of any one claim and in the aggregate in the Period of Insurance the sub-limit stated in the Schedule.

2. Accountants Clause

Any particulars or details contained in the Insured's books of account or other business books, documents or systems which may be required by the Underwriters for the purpose of investigating or verifying any claim hereunder may be produced and certified by the Insured's auditors or professional accountants and their certificate shall be prima facie evidence of the particulars and details to which it relates.

3. Extended Cover for Past Employees

Any person who ceases to be an Employee shall for the purposes of this Section be considered as being an Employee for a period of 30 (thirty) days after he ceased to be an Employee.

4. Expenses Incurred in Reinstating Office Records

This Section of the Policy is extended to include costs, charges and expenses incurred by the Insured in replacing and/or restoring any computer files, data, media, documents, manuscripts, business books, plans, designs, specifications or programmes destroyed, damaged or lost as a result of Loss insured by this Section of the Policy provided that the liability of the Underwriters shall not exceed in respect of any one claim and in the aggregate in the Period of Insurance the sub-limit stated in the Schedule.

MEMORANDA

1. In the event of the discovery of any Loss resulting from a Defined Event the Insured may notwithstanding anything to the contrary contained in General Condition 2 refrain from reporting the matter to the police but shall do so immediately should the Underwriters require such action to be taken.

2. It is understood and agreed that knowledge of his own fraud or dishonesty or that of others with whom he is in collusion by the person signing the Proposal and questionnaire or giving renewal or other instructions shall not prejudice any claim under the Policy.

3. **Unidentifiable Employees**

   If a Loss is alleged to have been caused by the fraud or dishonesty of any of the Employees, and the Insured shall be unable to designate the specific Employee or Employees causing the Loss, the Insured’s claim in respect of such Loss shall not be invalidated by their inability so to do provided the Insured is able to furnish evidence to prove to the reasonable satisfaction of the Underwriters that the Loss was in fact due to the fraud or dishonesty of an Employee acting alone or in collusion with others.

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