

When the going gets tough, do brokers get going?

When times are good, policies are being written and profits are high the relationship between re/insurance companies and brokers is usually cooperative and friendly. But when times get tough and an insurance company decides to go into run-off, a solvent scheme or is forced into liquidation/rehabilitation, obtaining broker co-operation can become difficult and sometimes contentious. For clarity's sake, the term run-off will be used for the remainder of this article to address all situations where the carrier is no longer writing business. The traditional relationship between re/insurance companies and brokers often lasted for decades. The expense of continuing to provide service for clients was offset by fees generated as new business was placed through the broker. Obviously, when a company ceases to write new business, the economics of the relationship change.

Document production and account reconciliation by the broker is particularly important in the context of run-off since often the largest problem for a run-off company in collecting or defending a claim is lack of documentation. In a typical run-off situation, a re/insurance company makes hundreds of document requests to its various brokers. These requests are typically for accounts relating to reinsurance receivables, one of the largest assets of a company in run-off. But when a broker has to prioritise between a claim submitted from a solvent, up-and-running insurance company from which they still receive compensation and a claim from an insurance company in run-off from which they typically receive nothing, there is a strong incentive for the broker to prioritise its workload to ensure the ongoing client receives service first. From the perspective of the company in run-off, this makes matters much more difficult. From the perspective of the broker, this is just sound business practice. This article explores some possible solutions to this problem, allowing for a much smoother and efficient run-off.

Strategy 1: run-off provision

One of the best ways to ensure a broker's co-operation is to include a run-off provision in the original contract. This

Obtaining broker co-operation can be one of the most troublesome aspects of implementing a smooth run-off, but measures can be taken to ensure the ongoing co-operation of all parties, says **David Presley** of Bazil McNulty.

allows the terms of the run-off to be negotiated prior to entering any contract, allowing the parties to create an agreement which works best for their particular situation. A run-off provision will also help define the broker's duties where the broker is surprised with a twenty year old claim on an account for which it hasn't received any compensation in decades. The run-off provision will typically provide for one of two things: (1) the terms of service between the broker and the

In the long run paying the broker will result in substantial savings in the form of a smooth run-off

re/insurance company in the case of run-off; or (2) provide for a broker replacement.

Discussing the terms of run-off service prior to it actually

occurring has several advantages. Firstly, it allows the broker to negotiate its compensation for servicing claims during the run-off period. This ensures that brokers are being adequately paid for their services during the run-off. Secondly, it will benefit the re/insurer because it allows the re/insurance company to know that they will have full broker support for the duration of any run-off. Thirdly, a run-off provision gives each party easily enforceable contractual rights if the other side does not follow the agreed upon terms. Setting predetermined run-off rights and obligations for both parties in the original contract can help reduce disagreements between brokers and insurance companies before they occur.

Strategy 2: broker replacement provision

Firms specialising in broker replacement are growing as the

number of both insolvencies and companies entering schemes of arrangement has increased. A broker replacement provision typically can be utilised where the original broker does not wish to continue servicing claims during a run-off. Broker replacement is an ideal solution to the broker co-operation problem because it serves the particular needs of both the re/insurance company and the broker. The original broker is content that it does not have to service decades old claims and the replacement broker is happy to assist with the run-off since it is being compensated for its work. One of the biggest downsides to using a broker replacement is transferring all the accounts to the new broker. Typically the documents are rather voluminous and transferring them to the new broker can be a tedious and complicated process. Done correctly, however, a broker replacement provision provides an excellent solution to the problem of obtaining broker co-operation.

Strategy 3: service agreement

Another way to obtain broker co-operation is to simply pay them for their services. This provides the broker with an incentive to investigate claims and accounts for re/insurance companies in run-off. Many re/insurance companies may view this as unfair since the broker already received compensation under the original contract. In the long run, however, paying the broker will result in a substantial savings in the form of a smooth run-off. Moreover, the cost may be less than the expense associated with litigation. The parties may enter into a service agreement which allocates payment in various ways, typically by either a flat rate (ie. paid to the broker quarterly, annually etc.), contingent on recovery (ie. ten percent of all claims collected with broker assistance), or a blend of the two (ie. flat rate plus five percent of all claims collected). Creating further incentives based on recovery, such as a 20 percent bonus on recoveries over a certain threshold, can further reward the diligence brokers put into their claims investigation. This is not to say that brokers will not give their best efforts without payment, but payment is a strong inducement to complete as thorough a job as possible. Obviously, these service agreements can be varied to suit the needs and particular situation of both the broker and the company in run-off.

Paying the broker is especially important in situations where the run-off or certain reinsurance assets of the Estate have been assigned to a third party. From a broker's perspective, although they may have received funds from the original re/insurance company, they have received nothing from the

assignee. In this situation, providing compensation to the broker is a great way to show appreciation for their efforts and will help build a stronger relationship between the parties.

Strategy 4: using arbitration to obtain the necessary documentation

A final and likely least efficient way of ensuring broker co-operation is for the run-off company to use the arbitration process to obtain any necessary documentation. As anyone in the reinsurance industry is probably aware, arbitration is the preferred method of dispute resolution. As such, it comes as no surprise that nearly every reinsurance contract will contain an arbitration clause. Inherent in an arbitration panel's authority to hear a case is also the authority to obtain necessary documentation from non-parties (brokers). In the

Obtaining broker co-operation can be one of the most troublesome aspects of implementing a relatively problem-free run-off

reinsurance setting this authority is based on the idea that brokers have an ongoing contractual and/or fiduciary duty to produce records on behalf of their clients despite the fact that they have not

received any compensation for years or possibly decades. Case law in the United States, although somewhat divided, provides support for the idea of this ongoing duty. Recently, in *Stolt-Nielsen SA -v- Celanese AG*, the 2nd Circuit Court of Appeals held that arbitrators could properly subpoena non-parties to produce various documentation under the Federal Arbitration Act ("FAA"). This ruling properly followed the plain language of FAA Section 7, which gives broad subpoena powers to arbitrators during an arbitration. Therefore, as a last resort a company in run-off can rely on the arbitration process to obtain any necessary documentation. Of course in reality using an arbitration panel's power to compel third parties to provide documentation is likely the least efficient way of obtaining the necessary documentation. Such a strategy requires the run-off company to needlessly incur the time and expense associated with initiating arbitration proceedings and utilising such a strategy sets a bad precedent for the relationship between the run-off company and the broker.

Round-up

Obtaining broker co-operation can be one of the most troublesome aspects of implementing a smooth run-off. By taking measures to ensure the ongoing co-operation of the parties, important issues such as maximising receivable recoveries can be addressed without interruption. This will result in a stronger and more co-operative relationship, minimising some of the largest problems associated with run-off.