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THE ROLE OF AN INSURANCE BROKER AND THEIR POSITION ON THE INSURANCE MARKET IN THE CZECH REPUBLIC

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Abstract

This paper focuses on the work of insurance brokers on the insurance market in the Czech Republic. It is based on the existing and former legislations and it focuses on a significant change that took place in the year 2005. On January 1, 2005 a new law on insurance brokers and self-employed adjustors came into force. The paper aims to analyze and compare the conditions for work of an insurance broker in the Czech Republic that exist now with those that had existed before the new law became effective. It evaluates the development in the numbers of insurance salesmen in relation to this legislative change.

Key words: *insurance broker, dealer activities, expert qualification*

JEL codes: *G22*

1. Introduction

The goal of my paper is to explain the conditions under which insurance brokers work on the Czech insurance market. It focuses on the following issues: the role of insurance brokers on the Czech insurance market, the analysis and comparison of the conditions for the job of an insurance broker according to laws that apply to them, the basic tasks of insurance brokers as per a special law that became effective in the year 2005, and the comparison of the numbers of insurance brokers (namely insurance salesmen) on the Czech insurance market since the year 2000.

Activities of insurance brokers as a part of the insurance market are not that visible. People who are interested in insurance or who already have one often do not even acknowledge that insurance brokers exist, or people perceive brokers in a wrong way. The client focuses on the insurance company as the main subject on the insurance market and thus is not familiar with the job of an insurance broker even though this job is now strictly defined by a law. The role of insurance brokers on the insurance market is very significant and this significance is even growing, as is the number of subjects who use the services of insurance brokers.

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2. Insurance brokers and their role on the Czech insurance market

Insurance brokers are subjects of the insurance market. Priority subject is an insurance company on the Czech insurance market. The insurance market is a part of financial market. Other subjects of the market include for example:

- Branches of foreign insurance companies,
- reinsurance companies/agencies,
- insurance brokers,
- associations,
- institution whose role is to observe the insurance sector,
- clients. ¹

Insurance brokers take part on the insurance market as an intermediary between the insured, insurant, and insurer. Their roles are quite broad. Aside from insurance offers they provide services to insurants in relation to risk management and counseling in many other financial issues. Insurance brokers are very significant aspect of the insurance market under the existing conditions. Thanks to their broad network of insurance agents they can actively seek potential risks that can be insured, by which they help insurance companies in improving their business results. Their attitude shapes the insurance market. ²

There are two inseparable parts of the insurance market:

- Material insurance market – represents the supply and demand in relation to the financial service of insurance.
- Investment insurance market – represents investments of available funds.

The sphere of business on the material insurance market includes:

- insurance activities,
- reinsurance activities,
- preventive activities,
- insurance broker activities (as defined by applicable law),
- activities that aim to support and develop the insurance industry, and to expand and improve its services. ³

1. MAJTÁNOVÁ, A. et al., Pojišťovnictví - teorie a praxe, p. 44.

2. ČEJKOVÁ, V., Pojistný trh, p.25.

3. DUCHÁČKOVÁ, E., Principy pojištění a pojišťovnictví, p. 161, 171.

3. Existing and previously valid legal norms that apply to insurance brokers

Rights and obligations of insurance brokers are now governed by the law number 38/2004 Coll. of December 17, 2003 on insurance brokers and self-employed adjustors in the Czech Republic. This law came into effect on January 1, 2005.⁴

Insurance broker is a legal entity or an individual who is involved in providing remunerated dealer activities in the insurance industry.

The new law does the following:

- it regulates the conditions under which insurance brokers and self-employed adjustors can conduct their business activities,
- it regulates the conditions under which insurance brokers and self-employed adjustors can launch their business activities,
- it establishes a registry of insurance brokers and self-employed adjustors,
- it sets out the conditions for regulation and oversight over the business activities of insurance brokers and self-employed adjustors.

The law number 38/2004 is a brand new and separate law for insurance brokers and it sets out clearly articulated obligations that have to be fulfilled on the part of an insurance broker. This law sets out significantly strict conditions and it lays emphasis on expert qualification of insurance brokers.

Activities of insurance brokers before January 1, 2005 were governed by the law number 363/1999 Coll. of December 21, 1999 on insurance industry.⁵

The law number 363/1999 Coll. governed the insurance sector, the conditions for insurance and reinsurance activities in the course of business, broker activities in the insurance sector, as well as the oversight of the state over these activities. Nowadays the law on insurance industry governs, as per the EU legislation, the conditions under which insurance and reinsurance activities are conducted, as well as the oversight over these activities and over the operation of pension insurance activities that is provided by the Czech National Bank.

4. Law number 38/ 2004 Coll.

5. Law number 363 / 1999 Coll.

4. Insurance brokers and their activities pursuant to law^{6;7}

4.1. Law number 363/1999 Coll. (valid until December 31, 2004)

Dealer activities in the insurance sector are expert activities leading to the conclusion of insurance or reinsurance contracts and related activities. These activities can be conducted by an insurance agent or insurance or reinsurance salesman. This applies only to those kinds of insurance that are administrated by an insurance company that has been given a license for insurance provisions pursuant to law, or by a reinsurance institution.

There are two kinds of insurance dealers:

- Insurance agent is a legal entity or an individual who conducts dealer activities in the insurance industry pursuant to a contract with an insurance company.
- Insurance or reinsurance salesman is a legal entity or an individual who conducts dealer activities in the insurance industry pursuant to a contract with a person who is interested in becoming a client and in concluding an insurance or reinsurance contract.

Clean criminal record is a prerequisite if a person wishes to work as an insurance dealer. Insurance or reinsurance salesman and insurance agent are required to have a liability for damage insurance for the performance of their duties for up to 5,000,000 Czech crowns. Insurance or reinsurance salesman must be registered at the Finance Ministry. There is no such requirement in case of an insurance agent. The state oversight in the insurance industry is conducted by the Finance Ministry.

4.2. Law number 38/2004 Coll. valid as of January 1, 2005

Dealer activities are expert activities that consist in the following:

- presenting of draft insurance or reinsurance contracts,
- preparation activities, the goal of which is the conclusion of insurance or reinsurance contracts,
- conclusion of insurance or reinsurance contracts in the name and on the account of an insurance or reinsurance company for which that particular agent/broker works,
- assistance in the insurance management and during claims to which an owner of insurance or reinsurance is entitled to.

6. Law number 38/2004 Coll.

7. Law number 363/1999 Coll.

Insurance broker is a legal entity or an individual who conducts broker activities for remuneration and in the insurance industry.

There are several types of insurance brokers:

- obligated insurance broker,
- subordinate insurance broker,
- insurance agent,
- exclusive insurance agent,
- insurance salesman,
- insurance broker whose home member country is not the Czech Republic.

Table in the Appendix 1 lists the comparison of particular insurance brokers and their rights and obligations pursuant to particular law, with the exception of the insurance broker whose home member country is not the Czech Republic.

4.3. Some key terms as per the law number 38/2004 Coll. relating to the activities of insurance brokers

Registry – Operated and maintained by the Czech National Bank. Individuals are listed in the registries according to their ID numbers. This registry is publicly accessible. Anyone can look into it and to make excerpts, transcripts and copies.

The news law stipulates that all insurance brokers be expertly capable. It means they should have the necessary knowledge, both general and expert-specific, that they need for their profession. Aside from this the law also strictly defines the term professional experience, by which it means work experience in an insurance company or in a reinsurance agency that relates to conclusion of insurance contracts, or in the capacity of an insurance broker in the insurance industry. General knowledge is proved by a high school diploma. Expert-specific knowledge is proved by a certificate of graduation from a specialized high school or university, or by taking expert exams. Every five years an insurance broker must attend a mandatory expert training to update their experience in the insurance industry.

Basic qualification level – expert qualification is not subject to professional experience.

Intermediate qualification level of expert qualification is subject to two-year professional experience.

High qualification level of expert qualification is subject to four-year professional work experience.

4.4. *Chart: contractual relations of an insurance broker pursuant to laws*

For visualization purposes see below to find a comparison of contractual relations among the client (insurant), insurance broker and the insurance company (insurer).

Chart number 1: Contractual relations pursuant to law number 363/1999 Coll.

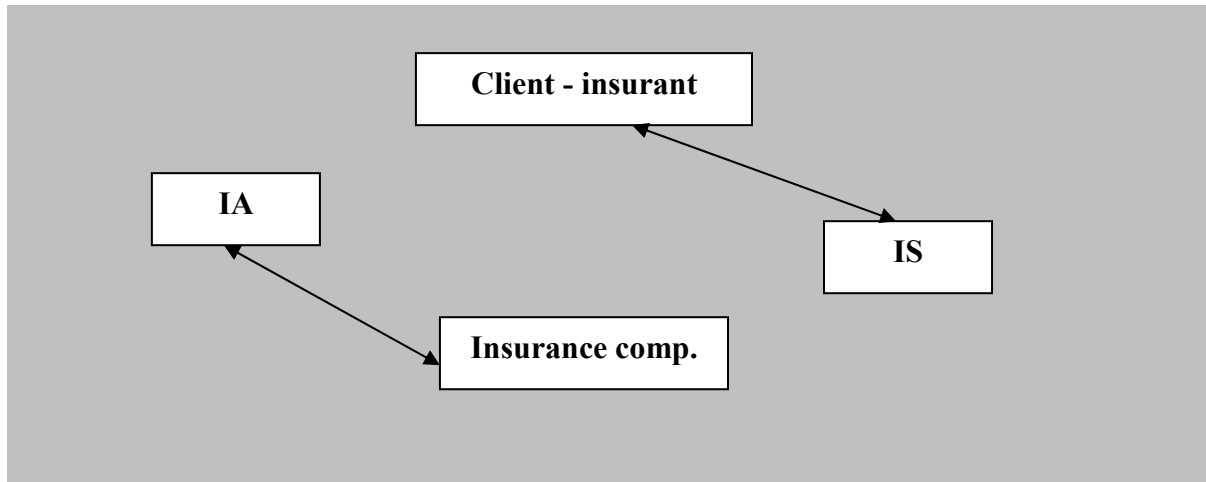
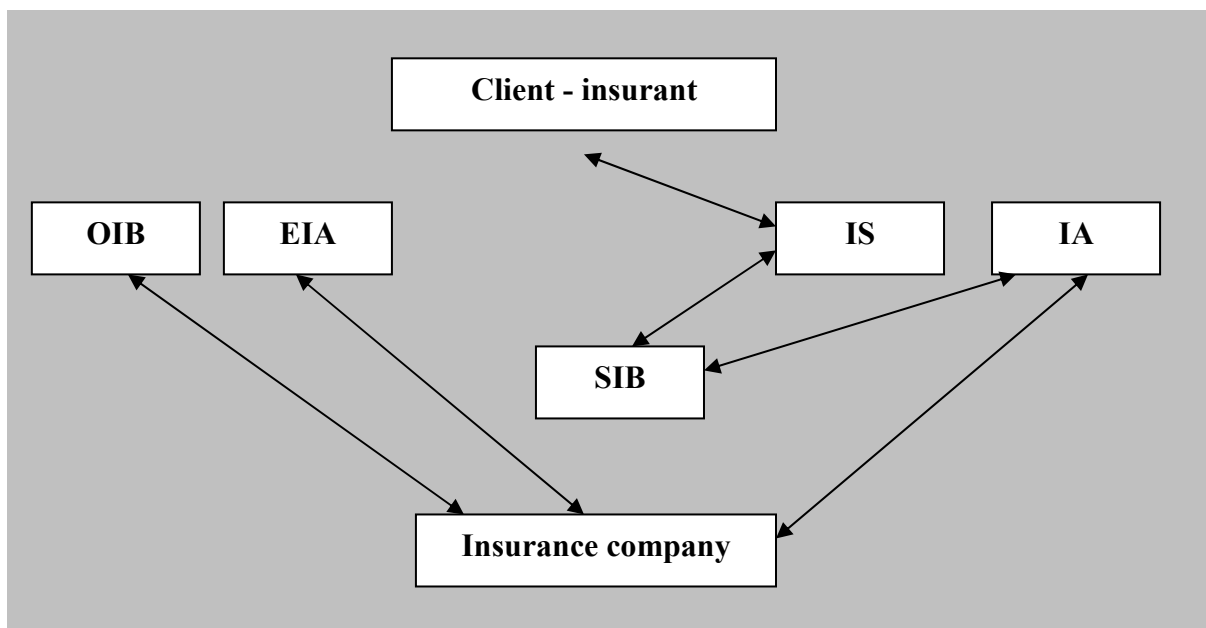


Chart number 2: Contractual relations pursuant to law number 38/2004 Coll.



The abbreviations used correspond with Appendix 1:

Obligated insurance broker (OIB)

Subordinate insurance broker (SIB)

Insurance agent (IA)

Exclusive insurance agent (EIA)

Insurance salesman (IS)

4.5. *Developments and changes in numbers of registered insurance brokers as a result of legislation change*

Table number 1: Development and changes in numbers of registered insurance salesmen between 2000 and 2004.

<i>year</i>	<i>Number of registered insurance salesmen</i>		
	<i>Individuals</i>	<i>Legal entities</i>	<i>Total</i>
2000	56	180	236
2001	88	249	337
2002	126	304	430
2003	159	367	526
2004	166	426	592

Source: Czech Finance Ministry, Insurance industry stat oversight, Annual report 2000 - 2004

Table number 2: Development and changes in numbers of registered insurance brokers after the legislation change.

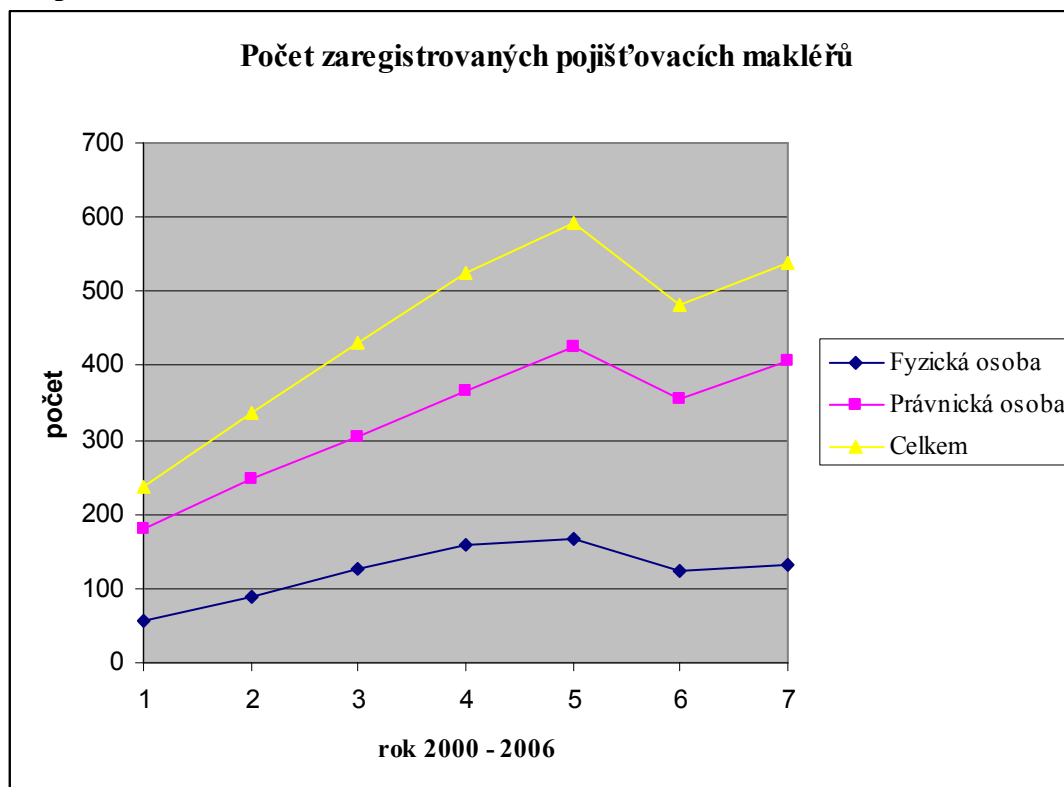
<i>Year</i>	<i>OIB</i>		<i>SIB</i>		<i>EIA</i>		<i>IA</i>		<i>IS</i>	
	<i>Ind*</i>	<i>l.e.*</i>	<i>Ind*</i>	<i>l.e.*</i>	<i>Ind*</i>	<i>l.e.*</i>	<i>Ind*</i>	<i>l.e.*</i>	<i>Ind*</i>	<i>l.e.*</i>
2005	5 707	576	17 259	576	9 837	42	427	425	125	356
2005 total	5 864		17 835		9 869		852		481	
2006	7 496	211	24 334	867	13 018	58	459	514	132	407
2006 total	7 707		25 201		13 076		973		539	

Source: Czech Finance Ministry, Dept. of Financial Market Analysis, Financial Market Development Report 2005-2006

*Ind – individuals

*l.e. – legal entities

Graph number 1: Demonstration of values from tables 1 and 2



Source: according to tables 1 and 2

Počet zaregistrovaných pojišťovacích makléř = number of registered ins. salesmen, fyzická osoba=individual, právnícká osoba = legal entity, celkem = overall, rok=year, počet = number

The figures shown above demonstrate that the number of insurance salesmen decreased with the legislation change that took place in 2005. The main reason is that the conditions under which they could work became more strict, as regulated by the law number 38/2004 Coll. When we compare the overall figures in years 2004 and 2005 we find out that it represents almost a 19-percent decrease. The conditions that were set by the new law were described in the previous sections of this article.

It should also be noted that the scope of activities of insurance salesmen, as the new law stipulates, is now broader. It includes the following conditions that are based on the content of a contract with a client:¹⁵

- elaboration of a complete analysis of insurance risks,
- insurance and reinsurance program(s) drafting,
- provision of consultative and advisory services,
- management of concluded insurance and reinsurance contracts,
- control of the revision deadlines of these contracts,
- cooperation in the process of insurance event settlement.

15. Law number 38/ 2004 Coll.

5. Conclusion

This article analyzes the role and position of insurance brokers as part of the insurance market in the Czech Republic. It compares the legislation that was in force before the year 2004 with that of 2005 and later. This analysis shows that the conditions under which insurance brokers worked since the year 2005 became stricter because of improvement of professional qualities of insurance brokers. The analysis also demonstrates that the law lays greater emphasis on the work of insurance salesmen as a subject on the highest professional level. Brand new law that applies solely to insurance brokers and adjustors represents stricter conditions in general in fulfillment of dealer activities. This fact also caused the decrease in the numbers of registered insurance salesmen.

Appendix number 1

<i>Obligated insurance broker (OIB)</i>	<i>Subordinate insurance broker (SIB)</i>	<i>Insurance agent (IA)</i>	<i>Exclusive insurance agent (EIA)</i>	<i>Insurance salesman (IS)</i>
Is under a written contract with insurance company.	Cooperates with IA or EIA or IS upon a written contract.	Is under a written contract with insurance company.	Is under a written contract with insurance company.	Is under a written contract with client interested in insurance.
Works for one or more insurance companies.	Obliged to follow instructions of broker he works with.	Works for one or more insurance companies.	Works for one insurance companies.	
Receives pay from insurance company. 2)	Receives pay from broker he works with.	Receives pay from insurance company	Receives pay from insurance company	Receives pay from insurance or reinsurance company
Does not collect insurance premium.	Does not collect insurance premium.	Is entitled to collect insurance premium 1).	Is entitled to collect insurance premium 1).	Is entitled to collect insurance premium 1).
Does not mediate payment of losses as per contracts.	Does not mediate payment of losses as per contracts.	Has the right to mediate payment of losses 1).	Has the right to mediate payment of losses 1).	Has the right to mediate payment of losses 1).
Offers presented from more insurance companies can not be competitive to one another.	Obliged to follow instructions of broker he works with.	Offers can be competitive in relation to one another.	Negotiates with one insurance company only.	
Insurance company is responsible for damage incurred in the course of work of a OIB.	Insurance broker on whose name and account the subordinate insurance broker works is responsible for damage this subordinate insurance broker causes in the course of his work - dealer activities in insurance industry.	Insurance agent is responsible for damage incurred in the course of his work. He must be insured with the limit of loss payments being 1,000,000 euros for one insured event and 1,500,000 euros for all insured events that occur in one insurance year.	Insurance company is responsible for damage incurred in the course of work of an EIA.	Ins. salesman is responsible for damage incurred in the course of his work. He must be insured with the limit of loss payments being 1,000,000 euros for one insured event and 1,500,000 euros for all insured events that occur in one insurance year.
Registered.	Registered.	Registered.	Registered.	Registered.
Fulfills credibility conditions.	Fulfills credibility conditions.	Fulfills credibility conditions.	Fulfills credibility conditions.	Fulfills credibility conditions.
Fulfills basic qualification level for expert knowledge.	Fulfills basic qualification level for expert knowledge.	Fulfills intermed qualification level for expert knowledge.	Fulfills basic qualification level for expert knowledge.	Fulfills high qualification level for expert knowledge.

¹⁾ Insurance agent, exclusive insurance agent and insurance salesman are required:

- to maintain cashable insurance capital in the amount of 4 percent of the overall amount of the insurance premium they collect, however, at least it should be 15,000 euros, or
- when transferring insurance premium or payments of losses they should use exclusively a special bank account that is independent of that used for the insurance worker's own business account.

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