Financial Services Authority

Transparency, disclosure and conflicts of interest in the commercial insurance market

December 2008
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This Feedback Statement reports on the main issues arising from Discussion Paper 08/2 (Transparency, disclosure and conflicts of interest in the commercial insurance market) and associated work. This is not a consultation document, but please direct any questions about this statement to:

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1 Overview

Introduction
1.1 This chapter sets out the overall context for our continued interest in wholesale commission disclosure, the management of conflicts of interest and transparency more generally in the commercial general insurance market.

1.2 Our statutory objectives require us to ensure that customers are appropriately protected and that confidence in the financial system is maintained. Our strategic aim of promoting efficient, orderly and fair markets is central to these objectives and is behind the importance we place on transparency. It is from this that our particular interest in the mediation of commercial general insurance stems. Our concerns are that:

- the blurring of lines between insurers and intermediaries creates the potential for conflicts of interest in this market; and
- commercial customers can be poorly informed about how (and how much) their intermediary is being paid and can be unclear as to the services being provided and the capacity in which their intermediary is acting.

Structure of this paper
1.3 In Chapter 2, we set out the background to our most recent programme of work and summarise associated developments we have taken into consideration. In Chapter 3, we set out the outcomes for commercial customers that we believe are appropriate and proportionate and how the industry guidance that is being developed will assist the market to achieve them. In Chapter 4, we present the findings of the three work streams that comprise our most recent programme of work (including feedback on our discussion paper) and set out how the findings give rise to the outcomes for customers.

Next steps
1.4 Our supervisors will be continually monitoring how firms are responding to the outcomes for customers. In 2010/11, we will be assessing whether customers are receiving sufficiently clear and comparable information about their intermediaries’ services, capacity and remuneration.
2 Background

2.1 Our concern with transparency in the commercial general insurance market is longstanding. In this Chapter, we briefly summarise the evolution of our work in this area and the actions arising. We also set out our most recent programme of work.

Conflicts management and commission disclosure

2.2 In February 2005, shortly after we began regulating general insurance intermediaries, we clarified our expectations concerning unfair inducements and the management of conflicts of interest.1

2.3 We followed this with thematic work to investigate how intermediaries were identifying and managing conflicts of interest. This found that many firms’ processes for identifying and managing conflicts were not sufficiently developed, and that firms’ often perceived conflicts of interest too narrowly. Around the same time, we identified that few commercial customers appeared to exercise their right under our existing rule to request details of the commission that intermediaries receive.2

2.4 In 2006, we undertook a further piece of thematic work to see if any improvements had been made. Our findings were encouraging in that firms’ processes for managing conflicts of interest had generally improved. However, disappointingly, we also found a widespread lack of formal processes amongst intermediaries to deal with customers requesting commission information.

2.5 In late 2006, we said we intended to undertake objective market failure analysis into whether a lack of transparency in the commission intermediaries receive gave rise to customer detriment and market inefficiency. We also set out our expectations regarding compliance with our current on request disclosure rule in a ‘Dear CEO’ letter.3

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2 The relevant rule is ICOBS 4.4.1: ‘(1) An insurance intermediary must, on a commercial customer’s request, promptly disclose the commission that it and any associate receives in connection with a policy. (2) Disclosure must be in cash terms (estimated, if necessary) and in writing or another durable medium. To the extent this is not possible, the firm must give the basis for calculation.’


4 FS08/7: Transparency etc in commercial insurance market (December 2008)
2.6 In March 2007, we commissioned CRA International Ltd (CRA) to undertake the market failure and high level cost benefit analyses\(^4\).

**CRA report – market failure and cost benefit analysis**

2.7 CRA was asked to consider whether a lack of automatic commission disclosure gave rise to a substantive market failure and, if so, whether mandating commission disclosure could be justified on cost-benefit grounds.

2.8 CRA identified commercial customers with a turnover of between £0.5 and £100 million (the 'middle-segment') as being at risk of detriment from non-disclosure of intermediaries’ commissions. These customers account for around £9.1 billion gross written premium per year, and represent about 50% of the UK’s commercial insurance market. They typically have complex needs and pay for mediation services through commission, although CRA found that many do not know how much commission their intermediary receives. When asked to guess, these customers estimated that the proportion of the premium intermediaries were receiving was around 10%, when they were actually receiving around 20% on average.

2.9 To determine the best way to address the market failures identified, CRA was asked to develop scenarios for mandating commission disclosure. It concluded that the cost of mandating commission disclosure earned throughout the distribution chain outweighed the benefits\(^5\).

2.10 However, CRA also identified wider issues about the market’s efficiency. These included commercial customers’ awareness of their right to request commission information and their understanding of the nature of intermediaries’ remuneration and services. CRA also identified changes in market practice and structure that heightened the importance of effective management of conflicts of interest.

2.11 In December 2007, we announced that the costs of mandating commission disclosure on its own appeared to outweigh the benefits and that we did not intend to introduce new requirements\(^6\). However, in response to the wider issues identified by CRA, we also outlined a programme of work on the management of conflicts of interest and transparency in the commercial general insurance market.

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\(^5\) This is described in CRA's report as 'Scenario 3A' (see page 97). The costs were estimated to be around £87m one-off and £34m ongoing. It was estimated that commissions of intermediaries servicing middle-segment customers would need to fall between 29% - 36% for the benefits to exceed the costs. However, CRA found that the likely impact of this scenario was a fall in commissions of only 10%.

2008 work programme – transparency, disclosure and conflicts of interest

2.12 In January 2008, we embarked on a wider programme of work aimed at assessing whether:

- intermediaries were managing conflicts of interest appropriately; and
- commercial customers were adequately informed about their intermediaries’ remuneration, capacity and services.

2.13 To assess whether these high-level objectives were being met, we divided the programme of work into three work streams. Feedback on the findings from these work streams is set out in Chapter 4.

Discussion paper

2.14 In March 2008, we published Discussion Paper (DP) 08/2, Transparency, disclosure and conflicts of interest in the commercial insurance market, which set out our concerns about the mediation of commercial general insurance and the outcomes (based on the evidence then available) that we would like to see achieved. It also set out three broad approaches for addressing our concerns and noted our willingness to consider an industry solution.

2.15 Interested parties had until 25 June 2008 to respond to the DP. We received 170 responses. A list of non-confidential respondents is in Annex 1.

Customer research

2.16 In April 2008, we commissioned IFF Research Ltd (IFF) to examine how commercial customers use information about intermediaries’ commission and services. Its aim was to test whether customers would benefit from clear and comparable information about the nature of intermediaries’ remuneration, the way in which they search the market and the capacity in which they are acting.

2.17 The research involved face-to-face interviews with 59 firms in the middle-segment identified by CRA as being at risk of detriment. The interviews took place in May and June 2008. IFF’s research report, including its methodology, can be found at: http://www.fsa.gov.uk/pubs/other/gi_disclosure.pdf

Thematic work

2.18 In May and June 2008, our Wholesale Firms Department undertook thematic work that sought to ascertain whether certain types of intermediary remuneration in the market and/or patterns of distribution gave rise to unmanageable conflicts of interest. The work involved surveying 47 intermediaries (representing £2.2 billion in commercial insurance income in 2007) and 21 insurers (representing £13 billion in gross written premium in 2007).
2.19 A summary of the thematic work’s methodology and findings is in Annex 2.

Other developments

2.20 Our willingness to consider a market based solution to the customer outcomes (see Chapter 3) has been informed by a number of other developments. These developments either have the potential to change the regulatory environment in the future, and so create some uncertainty for developing rules, or have recently changed it. They are briefly discussed below.

European Commission’s Business Inquiry Report

2.21 Our concerns about the transparency of mediated commercial general insurance and the management of conflicts of interest are similar to those raised by the European Commission in its inquiry report on business insurance in September 2007.8

2.22 The report concluded that a lack of transparency of intermediaries’ remuneration creates an environment in which the scope for competition may be reduced. It also raised concern that some intermediary remuneration arrangements, including contingent commissions, have the potential to lead to customer detriment and undermine competition.

2.23 The Commission’s Internal Market and Services Directorate General is currently looking into the report’s conclusions in the context of the implementation check of the Insurance Mediation Directive, with the intention of deciding at a later stage the most appropriate means of improving transparency in the commercial insurance market.

Law Commissions’ consultation paper

2.24 One concern we raised in the DP is customer understanding of the capacity in which their intermediary is acting and the link this has to the management of conflicts of interest.

2.25 In their July 2007 consultation paper, the Law Commission and the Scottish Law Commission argued that under the current law it is often unclear for whom an intermediary is acting at any given time. They provisionally proposed that:

- an intermediary should be treated as acting for the insurer, unless they are clearly acting on the customers behalf; and
- the law provide greater clarity about the capacity in which an intermediary is acting when obtaining pre-contract information.


2.26 The Law Commissions’ have identified support for some reform of business insurance law and will publish an issues paper setting out details of their proposals in the winter of 2008/09\textsuperscript{10}.

**Management of conflicts of interest: Changes to SYSC**

2.27 Ensuring that potential conflicts of interest in commercial general insurance are managed appropriately has, and will continue to be, a high priority for us.

2.28 Since we released the DP, we have published a Policy Statement that extends the requirements in our Senior Management Arrangements, Systems and Controls Sourcebook (SYSC), to a wider range of activities, including insurance mediation\textsuperscript{11}. These changes embed, and further clarify, our expectations about the systems and processes intermediaries and other regulated firms must have in place to manage conflicts of interest.


3 Our approach

3.1 This chapter explains our general approach to improving transparency in the mediation of commercial general insurance and the management of conflicts of interest.

Outcomes

3.2 In the DP, we set out our expectations in the form of six outcomes that we deemed appropriate to achieve a more efficient market. To determine whether these were the right outcomes for the commercial insurance market, we said we would base our thinking on the evidence gathered from responses to the DP and the findings of our thematic work and the customer research.

3.3 Based on this analysis, we have revised these into five outcomes for commercial customers, which we believe are proportionate and appropriate for this market. We encourage intermediaries to consider these outcomes when arranging their customers’ policies. The outcomes are:

(a) customers should have clear and comparable information about the commissions intermediaries receive;
(b) customers should have clear and comparable information about the services intermediaries are providing;
(c) customers should have clear information about the capacity in which an intermediary is acting;
(d) conflicts of interest arising from remuneration arrangements/business models should be properly disclosed and managed;
(e) commercial customers should have sufficiently standardised/comparable information to enable them to gauge the value of intermediary costs and services, and compare these across the market (and over time); and
(f) commercial customers should be made aware of their right to commission information and helped to appreciate the value of using it.

12 The six outcomes set out in the DP were:

a) Commercial customers should have information which indicates the full cost of mediation, including the likely extent of contingent commissions on a standardised and clear basis, and the total amount of commission paid to intermediaries throughout the chain;

b) Commercial customers should have clear information about the services an intermediary provides, including the breadth of search he undertakes;

c) Commercial customers should have clear information about the capacity in which an intermediary is acting (i.e. whether he is acting for them, for the insurer or, in some cases, for both);

d) Conflicts of interest arising from remuneration arrangements/business models should be properly disclosed and managed;

e) Commercial customers should have sufficiently standardised/comparable information to enable them to gauge the value of intermediary costs and services, and compare these across the market (and over time); and

f) Commercial customers should be made aware of their right to commission information and helped to appreciate the value of using it.
3.4 Our view is that if these outcomes are achieved, the process for arranging mediated insurance can become sufficiently transparent to allow customers to access the information they need to make informed decisions. We believe that this will address the risk of detriment to middle-segment customers and that, over time, it may also encourage more competitive and efficient distribution of commercial insurance.

3.5 Managing conflicts of interest is an essential part of the business of insurance intermediaries, and we continue to place great importance on firms having appropriate systems in place to manage them. However, our outcomes do not make reference to this as our:

- thematic work did not identify evidence of any systemic failings (see Chapter 4); and
- FSA Principles for Business (1, 6, 7 and 8) already provide a framework that firms must adhere to. As discussed in Chapter 2, we have also recently extended the scope of SYSC, which contains rules and guidance relating to the management of conflicts of interest, to insurance mediation activity.

3.6 Although we do not currently consider that additional measures to address conflicts of interest are required, we will continue to maintain close supervisory attention on their management, in particular on intermediaries with business models where the potential for conflicts is higher.

**Development of industry guidance**

3.7 Throughout the course of our work on the transparency of commercial general insurance, we have made it clear that we welcome the development of a market-led solution. This is consistent with our principles based approach to regulation, which means that (among other things) we:

- take a risk-based and proportionate approach to assessing the need for new rules;
- focus on outcomes and give firms flexibility to determine how best to meet them; and
- are open to the development of industry initiatives.

3.8 In the DP, we set out three broad approaches for meeting our (then) outcomes. We noted that we would welcome an industry solution, but recognised that stakeholder views – particularly regarding commission disclosure – were polarised.

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13 Principle 1: A firm must conduct its business with integrity; Principle 6: A firm must pay due regard to the interests of its customers and treat them fairly; Principle 7: A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading; and Principle 8: A firm must manage conflicts of interest fairly both between itself and its customers and between a customer and another client.
3.9 In May 2008, we hosted a round table discussion with trade associations, insurers and intermediaries at which we re-stated our view favouring a market-led solution. We have since been in ongoing discussions with the British Insurance Brokers’ Association, the London Market Insurance Brokers’ Committee and the Association of British Insurers (ABI) about outcomes for customers in this market.

3.10 We have been encouraged by these trade associations’ willingness to take a leading role in addressing the customer outcomes set out above. The result has been a commitment by them to develop industry guidance, much of which they intend to submit to us for endorsement as FSA confirmed guidance (the implications of this is summarised in Annex 3), for intermediaries and insurers.

3.11 Our view is that industry guidance has the real potential to lead to a change in the market and for the customer outcomes to be achieved. We welcome the:

- willingness of intermediary trade associations to actively encourage their members to adopt and adhere to the guidance they are developing; and
- support for industry guidance for intermediaries, including from the Institute of Insurance Brokers and the ABI.

3.12 We believe that if intermediaries adopt and adhere to the guidance that is being developed, it would neither be necessary nor proportionate for us to make rules to achieve the outcomes for customers. However, as we discuss below, we will keep this under review.

**How will we know if the outcomes for customers have been achieved?**

3.13 Moves to develop industry guidance are a significant and welcome step-forward. But for the outcomes to be met, intermediaries will need to act on the guidance by providing customers with clear and comparable information. To examine this, we will be monitoring progress towards the outcomes for customers. This will involve our supervisors, as part of their regular risk-assessments, asking firms about the actions they have taken in relation to the outcomes and about the reaction of their customers. We will also be asking the intermediary trade associations for regular updates on how they are going about promoting their guidance.

3.14 In 2010/11, we will assess whether the customer outcomes have been achieved. This is likely to involve:

- a survey of customers to assess whether they are receiving clear information about the nature of intermediaries’ services, capacity and remuneration and how they are using it (this is likely to be similar to, and build, on the independent customer research undertaken for us by IFF); and

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14 Any queries about the guidance for intermediaries should be directed to Steve White at BIBA (whites@biba.org.uk) or David Hough at LMBC (david.hough@lmbc.co.uk). Any queries about the guidance for insurers should be directed to Shradha Patel at the ABI (shradha.patel@abi.org.uk).
• review by our supervisors into firms’ awareness of the guidance and the changes they have made to business processes and systems in order to provide customers with clear and comparable information.

3.15 Within the context of our regulatory framework for managing conflicts of interest, we will continue to maintain close supervisory attention to those business models where we consider the potential for conflicts of interest to be greater; for example, firms with managing general agency (MGA) arrangements.
4 Feedback on our work programme

4.1 In this Chapter, we provide feedback on our most recent work programme into the transparency of mediated commercial general insurance and the management of conflicts of interest. This includes:

- feedback on responses to the DP;
- outlining the results of our thematic work on remuneration and distribution arrangements and their link to conflicts of interest; and
- outlining the results of the research we commissioned IFF to carry out on middle-segment customers.

4.2 As the three streams of our work programme overlap, we have structured this Chapter around six key themes. After each, we set out our response. The themes are:

i. operation of the market;
ii. remuneration arrangements;
iii. management of conflicts of interest;
iv. capacity disclosure;
v. service disclosure; and
vi. increasing client understanding: consistency, comparability and education.

4.3 We also provide feedback on stakeholders’ views on the possible approaches for responding to the concerns set out in the DP.

Operation of the market

4.4 In addition to identifying middle-segment customers being at risk of detriment from a lack of automatic disclosure of intermediaries’ commissions, CRA identified a wider set of issues with the potential to affect the efficiency of this market. This included transparency of the capacity in which an intermediary is acting and of the services being provided.
4.5 Our further work has not found evidence of significant market failure in the distribution of commercial insurance. In particular, our work does not suggest that there are any significant barriers to switching\(^{15}\). We also note that external research:

- does not suggest that the profits earned by UK insurers and/or intermediaries are significantly higher that that earned in other EU countries\(^{16}\); or
- there are barriers to entry for intermediaries, other than restricted access to the Lloyd’s market\(^ {17}\).

4.6 In the DP we asked:

Q1(i): Do you have any comments on CRA’s market-failure and cost-benefit analysis?

Q1(ii): Do the wider market efficiency issues highlighted in this paper affect the cost-benefit case for regulatory intervention, and how?

4.7 The following were among the few detailed comments we received:

- an independent survey conducted by a third party suggests that the figure of 50% of micro enterprises buying direct insurance is too high, so there may be market failure in this market segment as well; and
- CRA did not account fully for the competitive nature of the market, which allows customers to obtain cover for a variety of risks, so is in fact operating efficiently.

4.8 Respondents to the DP also believed that mandating commission disclosure could have the following unwanted consequences on competition:

- As customers would use commission information to shop around, intermediaries would need to spend more time tendering for new business. This would increase costs, but without any benefit in terms of better service or price as customers’ already have the information they need.
- The cost of mandatory disclosure could lead smaller firms to close, and cause consolidation in the market to accelerate, leading to reduced choice and service, and would allow larger intermediaries to demand higher commissions from insurers.
- While intermediaries would be required to disclose commission, insurers would not be required to make an equivalent disclosure, potentially creating an ‘uneven playing field’ between direct insurers and intermediaries.

\(^{15}\) The current level of switching is around 10% per annum, but this is not in itself a cause for concern. DP respondents and IFF’s customer research suggest that this relatively low level of switching is not necessarily linked to ‘weak’ competition, but because many customers are satisfied with the services provided.


\(^{17}\) The Lloyd’s market is currently the subject of HM Treasury led reform.
4.9 In addition, a number of respondents argued that the increased costs arising from a mandatory commission disclosure regime would simply be passed on to the customer. Some also questioned why we should consider providing commercial customers with commission information automatically when it is not required for ‘less-sophisticated’ consumers in the retail market.

4.10 We also asked:

Q11: What are your views on the practicability of the options we set out and their implications for competitiveness of the UK market?¹⁸

4.11 Many respondents argued that the UK market is already the most competitive in the EU. Around a quarter argued that mandatory commission disclosure would undermine this by increasing costs and so make it more difficult for UK intermediaries to compete in Europe.

4.12 Responses to Question 12, which invited comments on any other issues respondents thought we ought to consider, mainly restated the competition concerns raised in relation to Questions 1 (ii) and 11 noted above.

Our response

We believe that our focus on this market is warranted; our work programme has confirmed wider concern about the transparency of this market. We also note that the Law Commissions and the European Commission have raised concerns that are yet to be resolved.

Mandating commission disclosure

The development of guidance to address the outcomes for customers, including customers having clear and comparable information about their intermediaries’ commission, has had a significant bearing on our view of the need for a mandatory commission disclosure regime. We also note that most DP respondents, in particular intermediaries, did not support mandating commission disclosure and that CRA’s analysis of the case for mandating commission disclosure stood up well to scrutiny in our further work programme.

Costs of our outcomes

In our view, the costs of achieving the customer outcomes (whether through industry guidance or regulation) will not be sufficiently material to have a significant impact on competition.

We do not believe that customers having a greater understanding of intermediaries’ remuneration and/or their right to request commission information will generate the same costs to firms as mandating commission disclosure. As we discuss below, many customers do not currently place a high value on commission information. This means that significant assumptions would need to be made to link the marginal increase in systems costs to firms that may arise from greater customer understanding to the costs of a mandatory disclosure regime.

¹⁸ The three potential approaches are discussed at the end of this Chapter.
Uneven playing field

We do not believe that the outcomes risk creating an uneven playing field. Insurers, if they provide advice, normally advise only on their own products, so the service they provide is different from that provided by intermediaries. It is appropriate for disclosure standards for two groups of firms to be different if the services provided, and the risks to customers, differ.

Disclosure regimes

We have not changed our view of the appropriateness of having different commission disclosure requirements for commercial customers and retail consumers. Retail consumers generally have less complex needs (the products are often generic) than commercial customers. This, coupled with standardised products, makes it easier for consumers to compare and assess value-for-money. We also note that, unlike the commercial market, the level of shopping around is high for most retail products and there is competition between insurers and intermediaries across all market segments. Where we have identified significant consumer detriment in particular retail markets, we have introduced new requirements in ICOBS targeted at the sources of detriment.

Remuneration arrangements

4.13 CRA identified that customers typically underestimate how much their intermediary receives and may not understand how some forms of remuneration arrangements (for example, contingent commissions) operate. The DP also outlined concern about customer understanding of different types of remuneration arrangements. In addition, IFF’s customer research explored the way in which middle-segment customers responded to different types of remuneration information and how it was presented, and our thematic work looked into the prevalence of different types of remuneration arrangements.

4.14 In the DP we asked:

Q2: Do you agree that customers need to know the total remuneration earned by other intermediaries in the chain? If so, do you have any views on the logistics of providing the required commission information?

4.15 Most respondents disagreed with customers being told about remuneration earned by intermediaries throughout the chain. Reasons cited for this view included:

- customers only being interested in the total premium;
- the information would be additional to that already provided about the price and cover, and so would ‘overwhelm’ customers;
- the potential for this information to encourage customers to focus solely on the price of intermediaries’ services, rather than on cover and overall levels of service; and
• practical difficulties customer-facing intermediaries would face in getting remuneration information from other (wholesale) intermediaries in the chain.

4.16 Those in favour of disclosure said that customers need this information to fully understand the status and services of their intermediary.

4.17 In the DP we also asked:

Q3: Do you agree that contingent commissions should be disclosed in cash terms and on a comparable basis? If so, what do you consider to be the best way of doing this?

4.18 Most respondents disagreed with the idea that contingent commissions should be disclosed in cash terms and on a comparable basis. They noted that contingent commissions are paid on a book of business rather than on individual policies, so it can sometimes be difficult to work out the amount relevant to one particular customer. Practical difficulties involved in getting intermediaries ‘up the chain’ to provide information were also cited.

4.19 Those in favour of disclosure of contingent commissions said that disclosure on a cash basis (rather than, for example, expressed as a percentage) would be more meaningful for customers, and would require the least amount of time for intermediaries to explain.

4.20 Our thematic work found that:

• the use of contingent commissions is widespread, but they only represent a small proportion of intermediaries total income (approximately 1.5%); and

• only five of the 47 intermediaries sampled received more than 5% of their income as contingent commissions. These were mainly niche intermediaries.

4.21 IFF’s research into middle-segment customers found that:

• customers are more interested in the cover, services and premium of mediated commercial general insurance than in intermediary remuneration;

• of the 59 customers interviewed, half were aware of their right to request commission information;

• a third of the customers said they received commission information (16 automatically and three on request);

• customers preferred cash values to percentages for disclosure of contingent commissions; and

• customers became more interested in commission information as their understanding of remuneration structures increased as a result of their involvement in the research.

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Figures quoted are weighted as a percentage of commercial insurance income for 2007.
4.22 Most customers interviewed by IFF believed that they should be given commission information automatically; regardless of whether they would actually go on to use it. Customers cited the potential benefits of receiving commission as:

- reassuring themselves that the commission being paid is in line with their expectations;
- having more information with which to compare quotes;
- being able to assess whether or not they were getting value-for-money; and
- allowing them to negotiate their intermediary’s commission in order to reduce the overall premium.

4.23 Our thematic work found that the number of customers requesting commission information from the intermediaries in our sample is low. However, larger intermediaries tended to disclose commission to their large customers (as measured by premium) automatically.

**Our response**

In our view, customers should be alerted to their right to request commission information and should have access to clear and comparable information about the commission intermediaries receive. We believe that access to this information is important for customers who wish to shop around on the basis of commission information and/or who are interested in understanding intermediaries’ incentives.

**Current level of customer understanding**

We acknowledge that many customers currently appear uninterested in the commission their intermediaries’ receive. However, the current level of customer awareness about their right to request commission information is low. Customers involved in the research, although not new to buying insurance, placed greater value on commission information as their understanding of remuneration structures increased.

The customer research and the DP responses also suggest that limitations in the comparability of commission information may undermine its usefulness, and hence value, to customers (see below).

**Right to request commission information**

We believe it is appropriate for intermediaries to alert customers to their right to request commission in good time before conclusion of the contract. This will give customers time to exercise their right should they wish to do so. We also think it appropriate that customers be alerted in the same medium in which the policy has been arranged (for example, if it is over the telephone, then the customer should be alerted orally). And we think it appropriate that alerting customers form a prominent part of the sales process.

Customers tend to have long-standing relationships with their intermediaries. Given this, and to ensure that over time all customers are made aware of their right to commission information, we think it is appropriate that customers are reminded of their right to commission information at regular intervals (i.e. for new contracts and renewals).
Clear commission information

We believe that a customer having clear commission information means their intermediary explaining the different forms of commission they receive, both standard and contingent commissions. As above, we think it appropriate that these explanations form a prominent part of the sales process for new contracts and renewals. (We discuss how greater comparability of remuneration and other information can be achieved below.)

Management of conflicts of interest

4.24 Principle 8 requires a firm to manage conflicts of interest fairly. Our thematic work looked at firms remuneration structures and whether there were any that give rise to unmanageable conflicts. In the DP we said that:

Q5: We would welcome views on whether any particular arrangements/business structures give rise to unmanageable conflicts of interest.

4.25 No respondent who answered this question reported being aware of any arrangements or structures which created unmanageable conflicts. However, many respondents noted that there are several arrangements that require careful management (e.g. MGA agreements and delegated authorities), with a few suggesting that we tighten up our controls and supervision in this area.

4.26 Several respondents also thought that mandatory commission disclosure could even create conflicts of interest in the market by removing “Chinese walls” that have been put in place to manage conflicts of interest.

4.27 Overall, our thematic work suggests that most intermediaries are managing conflicts of interest appropriately, although there was scope for improvement amongst some firms. Intermediaries stated their use of procedure manuals and conflicts of interest policies, with most restricting knowledge of non-standard commission details to senior management, away from placing brokers.

4.28 CRA found that middle-segment customers were largely unaware of the potential for chains of intermediaries to arrange their policies and the potential implications this may have on intermediaries’ incentives. IFF’s customer research supported this finding. It found that few customers realised that there may be other intermediaries involved in placing their business. Once made aware of this, customers valued the information, in terms of reassuring themselves that their intermediary is acting in their best interests when deciding to use a chain. Our thematic work found that around 40% of commercial insurance by income is placed using a chain and that around a quarter is placed via a chain of more than two intermediaries.
Our response

In our view, customers should be made aware where there is a chain of intermediaries. Customers value information about the existence of chains, we believe correctly, as important to understanding the capacity in which the customer-facing intermediary is acting and the services being provided.

Management of conflicts of interest

Most of those who responded to the DP noted that although the potential for conflicts of interest is inherent in the industry, there are no particular business models that present unmanageable conflicts of interest. To the extent that intermediaries have adequate conflict management arrangements in place, we believe our thematic work corroborates respondents’ claims.

We feel that our current framework of principles and rules, including Principle 8 and recent changes to SYSC, are appropriate. We will, however, continue to pay close supervisory attention to the management of conflicts of interest, and will pay particular regard to intermediaries with business models that pose a higher risk.

Contingent commissions

We have not seen any evidence to suggest that contingent commissions have a significant impact on the risk of conflicts of interest. We note that they only account for a small amount of intermediaries’ overall income and that firms’ conflict management arrangements appear adequate. We also note that contingent commissions have the potential to generate positive benefits for insurers and customers by creating an additional incentive for intermediaries to accurately describe risks.

Existence of chains

We believe that, where chains exist, it is appropriate for intermediaries to make customers aware of them in a similar way to which they should alert them to their right to request commission; that is, before the conclusion of the contract and in the same medium in which the policy has been arranged. We think it appropriate that this form a prominent part of the sales process for both new contracts and renewals.

Capacity disclosure

4.29 In the DP, we outlined concerns relating to the extent to which customers understand the capacity in which their intermediary is acting. This information would enable customers to understand better the possible incentives the intermediary is working to. These concerns were echoed both by the responses we received and by the customer research.

4.30 In the DP we asked:
Q4: Do you agree that intermediaries should provide information on the capacity in which they are acting – i.e. as agent for the customer or the insurer or both? How should this be disclosed?

4.31 Many respondents believed that customers should receive this information, and a large proportion of intermediaries reported that they already provided it. They felt that customers should be informed of an intermediary’s capacity so they can be alert to potential conflicts of interest; this was seen as particularly important where the intermediary is acting for the insurer.

4.32 A very small number of respondents thought that disclosure of capacity was not necessary. Their view was that the default role of an intermediary is to act in the best interest of the customer, and that it is only if this relationship changes that customers need to be informed.

4.33 Views on the best way to make customers aware of the capacity in which the intermediary is acting ranged from including this information in Terms of Business Agreements (TOBAs) to disclosure at point of sale, along with a full explanation of the implications of the information for the customer.

4.34 In the DP we also asked:

Q6: Should we place any restrictions on what those describing themselves as ‘intermediaries’ can do?

4.35 The majority of respondents felt that there should be no restrictions on being designated an ‘intermediary’. Apart from practical and cost concerns, it was noted that existing ICOBS rules require disclosure of ownership interests and the extent of search. A widely held view was that as long as these rules are adhered to, additional restrictions are unnecessary.

4.36 Some respondents felt that some form of action might be justified, but not full restrictions on the use of the title ‘intermediary’. For example, it was felt that firms should not be able to use the title ‘intermediary’ if they only offer the products of one insurer.

4.37 A separate group of respondents thought that the use of the term ‘intermediary’ should be restricted. Their view was that intermediaries should be independent and unbiased with access to the best the open market can provide.

4.38 The IFF customer research showed that the capacity in which the intermediary is acting is something that many customers feel strongly about. It also found customers often misunderstood a number of the terms used by intermediaries to disclose the capacity in which they are acting. However, this was coupled with a finding that as things currently stand, customers are unlikely to request this information specifically.

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20 For example, under ICOBS 5.3.1 R, an intermediary must take reasonable care to ensure the suitability of its advice for any customer who is entitled to rely upon its judgment.

21 See, for example ICOBS 4.1.2 R, which relates to disclosure of an intermediary’s interests, and ICOBS 5.3.3, which relates to advice on the basis of a fair analysis of the market.
The use of the term ‘broker’ was previously subject to regulation under the Insurance Brokers Registration Act 1977. This restriction was repealed around the time that Financial Services and Markets Act 2000 came into force. Despite its apparent importance to them. This seems to be because they assume the intermediary is acting solely on their behalf. The research did find that when clients had a better understanding of the information, many indicated that they would use it.

**Our response**

In our view, customers should be given clear information about the capacity in which an intermediary is acting.

DP respondents, and firms sampled in our thematic work, widely agreed that improvements could and should be made to the way in which intermediaries describe the capacity in which they are acting. Our research found that many customers do not realise that the intermediary may be acting in different capacities, but once made aware of this, saw this information as important. However, we also recognise that the capacity in which an intermediary is acting can be unclear in some situations.

We believe that a customer having clear information means their intermediary explaining whether they are (or will be) their agent, or that of the insurer, over the life of the policy. In explaining the life of the policy, we believe it appropriate for the intermediary to set out those key junctures where they believe the capacity in which they are acting may change (for example, in the event of a claim). If the intermediary is concerned that their capacity is unclear, then we believe it is appropriate for them to explain their relationship with the insurer to the customer (for example, by setting out all of the paid services they undertake for the insurer). Again, we believe it appropriate for the customer to receive this information in good time before conclusion of the contract and that it form a prominent part of the sales process for new contracts and renewals.

**Use of the term intermediary**

We note that previous attempts at placing restrictions on the designation ‘intermediary’ have been abandoned owing, in part, to regulatory avoidance. Taking this past experience and the DP responses into account, we will not be seeking to limit what activities those describing themselves as ‘intermediaries’ are/are not allowed to carry out.

**Services disclosure**

4.39 CRA found a lack of customer understanding of the services that intermediaries provide. IFF’s customer research and the questions posed in the DP sought to gather further information on this issue, in particular the extent to which customers are aware of how intermediaries are searching the market on their behalf.

4.40 In the DP we asked:

Q7: Do you have any views on how we might best improve customers’ understanding of the breadth of search undertaken by their intermediary?

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The use of the term ‘broker’ was previously subject to regulation under the Insurance Brokers Registration Act 1977. This restriction was repealed around the time that Financial Services and Markets Act 2000 came into force.

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22 FS08/7: Transparency etc in commercial insurance market (December 2008)
4.41 The majority of respondents said that they already fully disclose the terms on which they search the market in their TOBAs. Some respondents felt that any specific requirement to specify the number of quotes obtained could be misleading, since the intermediary’s experience and knowledge of the best firms to approach for a given risk is arguably more important than the number of firms approached.

4.42 Some respondents who felt that improved disclosure would be beneficial noted that customer education on the capacities in which an intermediary may act, and on the associated terminology, could be more beneficial than regulatory intervention. It was also noted that ICOBS rules are already well established and adequately worded. Increased supervision and enforcement activity was also viewed as being sufficient to address any issues arising from a lack of clarity.

4.43 Those respondents who said that intermediary experience is the most important factor said:

- Breadth of search is much more relevant in relation to some commoditised general insurance products. With more technical covers, expertise is demonstrated by advising on insurers contacted, details of pricing and cover, together with reasons for advice. It is important to demonstrate that care is taken to ensure customer satisfaction, not just the cheapest possible quote.

- It is important to improve customer understanding, but it would be counter-productive if intermediaries started seeking additional quotes just so they could tell the customer that they had conducted a wide search. A skilled intermediary should know the market sufficiently well to know that there is little point placing certain risks with certain insurers.

4.44 IFF’s customer research found that in general, customers would prefer their intermediary to search the entire market when placing their business as they feel this is likely to get them the best quote; at the same time they realise that this is not always practical. Despite this, it found that a minority of customers recognised that intermediaries may be able to get better deals through having close relationships with insurers.

4.45 As with capacity disclosure, IFF’s customer research showed that many of the terms used in typical disclosure documents were interpreted in a number of (often incorrect) ways by customers, suggesting that greater clarity of terminology and better client understanding would be of benefit.

**Our response**

Our view is that customers should have clear and comparable information about the services provided by intermediaries, including the nature and breadth of the search conducted.

Respondents generally agreed that improvements should be made to the way intermediaries describe their services. IFF’s customer research demonstrates that middle-segment customers attach great importance to receiving clear information about the basis on which intermediaries search the market.
We believe that our current requirements in ICOBS provide an appropriate basis for providing customers with clear information about how an intermediary is searching the market on their behalf. However, we believe it appropriate that this information be given greater prominence in the sales process both for new contracts and renewals so that customers are aware of it and are able to ask about its implications.

**Increasing customer understanding: Consistency, comparability and education**

4.46 We made several suggestions in the DP regarding improving the comparability and clarity of information that is disclosed to customers. This was one of the areas of focus of IFF’s customer research, which found it affected the way in which customers select intermediaries and use the information given to them.

4.47 Moreover, anecdotal evidence suggests that customers typically do not take the time to read through TOBAs and that intermediaries tend not to focus on its content as part of the sales dialogue. Also, TOBAs can be long and complex documents, creating a risk that the information that customers may wish to refer during a sale is 'buried'.

4.48 In the DP we asked:

Q9: We have made several suggestions in the paper about how to improve the comparability of information on both remuneration and services. Which of these do you think is likely to be most effective? Are there any other approaches you believe we should consider?

4.49 The majority of respondents who commented on this issue felt that some form of ‘standardisation’ would be beneficial.

4.50 Those who disagreed said that standardisation could stifle innovation, and that the approaches described run counter to our principles based approach to regulation.

4.51 The customer research found that many customers who received standardised information found it easier to compare quotes and intermediaries. Half of the participants stated that if the information were in a standardised format, they would be more likely to make comparisons in the future. However, the research also found that this was most likely among customers who already placed some value on the information being provided in the first place. The research concluded that standardisation, by itself, was unlikely to change the behaviour of customers who currently place no value on the information.

4.52 The customer research also noted that standardisation of content without standardisation of format was less valuable to customers. Customers reported that it was much easier to ‘learn to read’ one type of document and extract useful information than it was to have the same information about different quotes.
displayed in different formats. This is particularly true of those who do not fully understand the context of the information they were provided with.

4.53 Importantly, the customer research found that customers were unwilling to pay for standardised information, despite the fact that they valued it. This was because they believed the costs of providing it would be small and that intermediaries should be able to absorb them.

4.54 The customer research recommended strongly an education initiative of some kind, stating that customers need to be helped to appreciate the information available to them before they would start using it. This idea was put forward in the DP and a number of respondents put forward views on this subject.

4.55 In the DP we asked:

Q8: To what extent do you think we could rely on a customer education initiative to help customers understand the value of information about commission and services?

4.56 The majority of DP respondents did not think such an initiative would be effective. However, several thought that it would be of value. Those respondents that disagreed with an education initiative said:

• commercial customers are sophisticated/knowledgeable enough already or would be unable to understand the technical detail;

• it would be too costly and these costs would eventually be passed on to customers; and

• this would be out of proportion with the level of assistance given to less-sophisticated retail consumers.

4.57 Those respondents who were in favour of a customer education initiative said:

• an informed customer is better placed to judge value-for-money;

• it would reinforce the other elements of the ‘solution’, increasing the likelihood of success; and

• it would be a far less costly alternative to mandatory disclosure.

4.58 IFF’s customer research also highlighted a need for increased levels of customer knowledge. It suggested that a customer education programme would help maximise the gains of increased comparability. It is clear that its research had a ‘learning effect’ on customers who, as they became more knowledgeable about the information being presented to them, became more interested in the ways in which they could use it to obtain lower premiums.
Our response

In our view, customers should have clear information and when provided it should be in a form that aids comparability to help improve their understanding about intermediaries’ remuneration and services.

Comparability

IFF’s research demonstrates that the benefits of providing information to customers in order to increase their understanding are likely to be greater when the information is provided in a manner that is clear and comparable. We believe this is likely to be particularly true for smaller businesses where the person purchasing the insurance product is not an insurance or risk expert.

We recognise that providing information in a manner that aids comparability requires some degree of ‘standardisation’. This is something that no one intermediary can achieve by itself and requires a degree of consensus across the industry. As we set out in the DP, we also recognise that there is a continuum of approaches that can be taken to standardisation, ranging from the use of common definitions through to prescribed forms.

We believe that providing information in a manner that aids comparability means that intermediaries assist customers by using common phrases and/or templates that will make it easier for customers to understand information over time.

Education programme

Our current view is that we do not need what would be a necessarily time-limited, and likely expensive, education programme. We believe that the revised customer outcomes, if achieved, will be effective in raising customer understanding over time.

Informing our approach to a solution

4.59 In the DP, we outlined three possible approaches for addressing the concerns we raised. These were:

i. improve the current regime through more rigorous supervision and enforcement of our existing rules and principles, plus guidance and a customer education initiative;

ii. an enhanced ‘on-request’ commission disclosure regime; and

iii. mandatory commission disclosure.

4.60 The DP also explored three further options which were capable of being delivered under one, or more, of the approaches listed above:

- making information easier to compare (for example, common definitions, principles for describing certain types of remuneration arrangements or standardised commission disclosure templates);

- improving the way firms mitigate conflicts of interest (for example, requiring clearer, more explicit disclosure about who the intermediary acts for and in what capacity); and
• improving customers understanding of the extent of search carried out by an intermediary (for example, by requiring intermediaries to inform their commercial customers of the number of quotes they obtain).

4.61 In addition, we also set out our willingness to explore the possibility of an industry solution for some or all of our concerns.

4.62 In the DP we said:

Q10: We would welcome comments on the relative merits or drawbacks of the three broad approaches outlined in Chapter 5. What other approaches (or permutations), if any, should we consider?

4.63 Many respondents to the DP felt that the first possible approach, more rigorous supervision and enforcement of our existing rules, would be the best approach for us to take. This was because they felt that the existing rules were adequate to meet our concerns, if applied in a slightly different way. However, some also felt that changes are needed, and that any supervisory response would need to be significant if it were to achieve the desired outcome.

4.64 The second possible approach, an enhanced on-request regime (including new industry or FSA guidance), was viewed as appropriate by a number of respondents.

4.65 The third possible approach, mandatory commission disclosure, was felt by a significant majority of DP respondents to be a disproportionate response to the problem.

4.66 Few respondents commented on the supplementary options set out in the DP. Those that did referred to previous comments made about standardisation, the management of conflicts of interest and customer understanding of the search being undertaken by intermediaries.

4.67 A number of respondents, mainly trade associations, called for an industry solution to address the concerns raised in the DP.

**Our response**

As we set out in Chapter 3, our current view is that if firms follow the industry guidance that is being developed then an environment will be created in which the process for arranging insurance can become more transparent. We believe allowing time for intermediaries to achieve the outcomes for customers is a proportionate and appropriate approach, but will reassess this if transparency has not improved. We would then need to consider a full range of approaches and options for achieving the outcomes for customers.
Annex 1

List of non-confidential responses to DP08/2

Access Underwriting Ltd
AIG UK Ltd
Alan Boswell – Managing Director (Alan Boswell Group Ltd)
Alan Boswell Insurance Brokers & Alan Boswell Insurance Services Ltd
Allianz Insurance plc
Alpine Insurance Services Ltd
AON Ltd
Association of British Insurers
Association of Insurance and Risk Managers
Association of Lloyd’s Members
Association of Residential Managing Agents Ltd
Atrium Underwriters Ltd
Aviva Plc
AXA UK Ltd
Bartlett & Company Ltd
BGL Group Ltd
Bickley Insurance Ltd
Blake Marston Priest Insurance Consultants Ltd
BMS Group Ltd
Brett & Randall Insurance Brokers Ltd
Bridge Insurance Brokers Ltd
Brit Insurance Ltd
British Insurance Brokers’ Association
British Property Federation
Broadhurst & Co. Insurance Brokers
Broker Network
Brokerbility Ltd
Bruce Stevenson Risk Management Ltd
Burgess Thompson & Richardson Ltd
Callaway & Sons Insurance Consultants Ltd
Cardal Assurance
Caunce O’Hara & Company Ltd
CBG Group plc
Central Insurance Services Ltd
CETA Insurance Ltd
Chaucer Syndicates Ltd
Clark Thomson Insurance Brokers Ltd
Clear Insurance Management Ltd
Cooke & Mason Plc
Coversure Insurance Services Ltd
Create Solutions Ltd
D. Barnett (Brokers) Ltd
Davis Corporate Risks Ltd
De Ford Insurance Brokers Ltd
E Coleman & Company Ltd
Endsleigh Insurance Services Ltd
F&C Property Asset Management Plc
Federation of European Risk Management Associations
Giles Insurance Brokers Ltd
Great Lakes Reinsurance (UK) Plc
Greg Knight MP
Harry Fort Insurance Brokers
Hawthorne Parkes Ltd
Hayes Parsons Ltd
Henderson Insurance Brokers Ltd
ICB Consultancy Services Ltd
Institute of Chartered Secretaries and Administrators
Institute of Insurance Brokers
International Underwriting Association of London
James Hampden Insurance
Jardine Lloyd Thompson UK Ltd
JC Roxburgh & Co. Ltd
Jefferey Associates
Jelf Group plc
John Ansell & Partners Ltd
K Burton & Son Ltd
Kerry London Ltd
Knightsure Insurance Brokers Ltd
Layton Blackham Insurance Brokers Ltd
Lexham Insurance Consultation Ltd
LFC Insurance Brokers Ltd
Liberty Mutual
LIBG Ltd
Linda Riordan MP
Liverpool Victoria
Lloyd & Partner Ltd
Lloyd’s
Lloyds Market Association
Localsprint Ltd
Lockton Companies International Ltd
London Market Insurance Brokers’ Committee
Lucas Fettes & Partners Ltd
Luiker Rowe Hibernian Ltd
Lymm Insurance Brokers Ltd

Annex 1
M J Pountney
Managing Agency Partners Ltd
Mark Taylor (Coversure)
Mark Hunter MP
Mark Prisk MP
Miller Insurance Services Ltd
Moreland Insurance
Morrison Insurance Solutions
Neville Insurance Consultants Ltd
Norman Butcher & Jones Ltd
Osmond Davies Insurance Brokers
Oval Ltd
Owen & Ewing Insurance Brokers
Park Home Insurance Services Ltd
Pennant Insurance Services
Perkinsslade Ltd
Peter Atkinson MP
Peter Hoare & Company (Insurance Brokers) Ltd
Philip Williams & Co Insurance Management
PJ Franklands Ltd
Douglas Insurance Service
PJ Weller & Son Ltd
Priest & Co. Ltd
ProAktive Risk Group
R.K Henshall & Co Ltd
R.K. Carvill & Co. Ltd
Reich Insurance Brokers
RIB Group Ltd
Roger Smith Insurance Brokers Ltd
Roland Smith Ltd
Romero Insurance Broker Ltd
Royal & SunAlliance Insurance Plc
Royal Institution of Chartered Surveyors
Ryan Insurance Group Ltd
SBJ UK Ltd
Shearwater Insurance Service Ltd
Skirrow Insurance Services
Small Businesses Practitioner Panel
Smart & Cook Ltd
Strathtay Insurance Brokers
Stride Ltd
Stuart Alexander Ltd
Sutcliffe Solloway & Co Ltd
T H March & Co Ltd
T. Henderson Insurance
Ten Insurance Services Ltd
The City of London Law Society
The Institute of Insurance Brokers
The Royal Bank of Scotland Plc
Stephen Dorrell MP
Thompson & Richardson (Lincoln) Ltd
Thompson & Richardson Ltd
Thompson Health and Bond Ltd
TL Dallas & Co. Ltd & TL Dallas (City) Ltd
Todd & Cue Ltd
Towergate Risk Solution (Sevenoaks)
Towergate Risk Solution (Taunton)
Towergate Risk Solutions (Kettering)
Towergate Risk Solutions (Newquay)
Turner Rawlinson & Co Ltd
Tyser & Co Ltd
UK Facilities Plc.
United Insurance Brokers Ltd
Venture Preference Ltd
W.B Tidey & Company Ltd
Webb Holton & Associates Ltd
Willis Group Ltd
Zurich Financial Services (UKISA) Limited

We also received responses from 13 insurance firms/intermediaries and two professional bodies who asked that their replies remain confidential.
Thematic work is one approach we use to supervise regulated firms. It involves analysing a particular product or practice to see if there are widespread issues that we should act upon.

This annex summarises the objectives, approach taken and findings of our thematic work into the types of remuneration and the management of conflicts of interest in mediated commercial general insurance. We also set out general observations made during the course of our work.

**Objective**

We worked to ascertain the types of remuneration currently operational within the commercial insurance market, and the patterns of distribution, in order to assess whether they might give rise to unmanageable/unacceptable levels of conflicts of interest that cause customer detriment.

**Approach**

The thematic work was conducted in May and June 2008. It involved:

- 47 intermediaries, representing £2.2 billion in commercial insurance income in 2007, completing a detailed questionnaire. Intermediaries were selected to provide a representation of large, medium and small firms, from both the London and regional markets; and

Note that in order to maintain confidentiality, and owing to the characteristics of this market, we have not provided a detailed breakdown of firms surveyed either by market or size.
• 21 insurers, representing over £13 billion in gross written premium for commercial clients in 2007, completing a similar questionnaire. The purpose of interviewing insurers was to provide a source of comparative information.

**Key findings**

**Remuneration**

We found that the use of non-standard commissions/fees in the UK commercial insurance market is widespread – 75% of intermediaries and 85% of insurers in our sample. However, the proportion of intermediaries’ income that contingent commissions represent is small, around 1.5%. The firms that had more than 5% of their income from non-standard commissions were niche businesses. Only one intermediary in our sample, and five insurers, had/operated volume over-rider agreements.

Overall, we found no discernable patterns of remuneration by class of business (i.e. by size and/or market). Those firms that use profit commissions and other types of non-standard commissions/fees represent all sizes of firms, from across the London and regional markets.

**Distribution**

We found that over 80% of intermediaries were operating delegated authorities from insurers, with 10% of intermediary firms sampled acting under managing general agency (MGA) arrangements (57% of the insurers said that they operated MGAs). We also found that around 8% of intermediaries’ remuneration is earned under a delegated authority.

There was extensive use of chains amongst our sample of firms, both in the UK and extending overseas. Of the five brokers sampled that did not place business via a chain, three operated in niche domestic markets. Overall, around 40% of commercial insurance business is via a chain, 13% of which is in a chain of more than two intermediaries.

**Management of conflicts of interest**

We found no indication amongst our sample of firms that the use of non-standard commissions/fees presented unacceptable conflicts of interest. Nor was there any evidence of endemic or systemic failings in managing conflicts of interest.

The approach employed by firms to manage conflicts of interest that have the potential to arise from different forms of remuneration and distribution appears to be effective and embedded appropriately within most firms sampled. Firms stated their use of procedure manuals and conflicts of interest policies, and most restricted knowledge of non-standard remuneration details to senior management, away from placing intermediaries.

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Figures quoted are weighted as a percentage of commercial insurance income for 2007.
Our work does not suggest that the potential conflicts of interest that may arise from delegated authorities is likely to be of particular concern. Only 6% of the intermediaries sampled had full underwriting authority (20% limited), with 1% having full claims authority (5% limited).

**General observations**

**Remuneration**

Our work suggests that intermediaries’ income earned from fees from work transfer arrangements is very low, although feedback from our supervisors suggests that firms are looking to increase income earned in this way.

Premium finance was provided by about a third of the firms in the sample, across all markets. Some of the larger intermediaries charge for ‘risk consulting’ or indicate earnings from ‘other fees’.

**Distribution**

Amongst our sample of firms, MGA agreements appear to be on the increase – 19% of intermediaries said that were contemplating setting one up, while half of the insurers said they were considering setting up more.

**Commission disclosure**

Of the intermediaries sampled, most only disclosed commission on-request in line with our current requirements. However, the number of requests was very small (representing around 1.8% of customers by income).

‘Automatic’ disclosure seemed to be dictated by the size of the client, with some of the larger intermediaries indicating that they always disclosed their commission to their ‘big’ clients (as measured by premium).
Role and status of confirmed industry guidance

In line with our more principles-based approach to regulation, we welcome industry initiatives which help those who want more support in exercising judgement about suitable means to meet our regulatory requirements – whether that be case studies, fact sheets, ‘questions and answers’ or more traditional forms of guidance.

In September 2007, we published Policy Statement 07/16 (Financial Services Authority. Confirmation of Industry Guidance), which detailed our policy and process for endorsing (‘confirming’) industry guidance, including the practical effect it has for firms’ compliance with our rules. Although it is not compulsory for firms to follow industry guidance we have confirmed, we do give assurances that if a firm follows the guidance correctly, and it was appropriate for them to do so, we ‘... will not take action against a person for behaviour that it considers to be in line with guidance ...or FSA confirmed industry guidance’.

For us to confirm industry guidance, certain criteria must be met. These state that industry guidance:

- that will directly affect consumers must consider consumer views and interests;
- must be made publicly available;
- should explain how it relates to a relevant FSA rule and/or principle;
- must be optional and be one way, not the only way, to comply;
- must not claim to limit or affect the rights of third parties;
- must detail which firms it is intended for; and
- must not be anti-competitive.

We cannot confirm guidance that goes beyond our existing rules and principles. Where the guidance suggests practices that go beyond our existing requirements, we require that it be clearly identified as such, so that firms can decide whether to follow it.

Guidance we confirm is valid for three years, after which confirmation status will be revoked, unless the industry asks us to renew it.

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27 Decision Procedures and Penalties Manual (DEPP), 6.2.1(4) G
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