Scientia Compliance Ltd
Compliance & Risk Management Services

COMPLIANCE NEWS

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Editorial

So should commission be disclosed to commercial customers or not as a matter of course? The guidance doesn't actually say anywhere that commission must be disclosed to commercial customers. However the standard templates that the market bodies want firms to use do make it clear that numerical values should be attributed to all direct and indirect earnings and disclosed in full. So it is clear in which direction firms are being nudged so at the very least it has to be made abundantly clear that a commercial customer has a right to know how much he is being charged for his policy. Good luck to all those who have to sit down and work out any profit commission that could be earned on a per policy basis!

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Further information on the issues in this newsletter, or any other issues which concern your business, can be obtained from Chris Keene on 020 7369 5375 / 07775 610006

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

As we know the FSA has concluded that it will not make rules on commission disclosure on the basis that the market has come up with its own solution. This has resulted in the development of industry guidance which has been reviewed by the FSA. This is not FSA guidance but in practical terms the FSA will take compliance with the guidance into account if a firm breaches its requirements.

The guidance includes model wordings and it strongly recommends the use of these wordings to reduce the risk that firms will inadvertently breach the FSA's requirements. The guidance also states that it will make it easier for commercial customers to understand the role and approach of one firm compared to another.

Below are a few key points that intermediaries that have direct client contact with the commercial customer will have to consider:

1) Intermediaries must make it very clear to customers about the services that they provide, including the breadth of search they undertake when searching for an appropriate insurance policy;

2) The customer must be informed when another intermediary has been involved in the placing of their business;

3) If an intermediary provides a service based on 'fair analysis' then an intermediary's analysis of the market should be kept up-to-date to ensure that offerings to clients are appropriate;

4) An intermediary needs to be able to have examined a sufficiently large number of insurance contracts available if it is giving advice on the basis of 'fair analysis'.

5) If the intermediary uses a panel of insurers to select a policy then the panel selection criteria should be sufficient to meet the 'fair analysis' criteria. This criteria could include remuneration to the intermediary but should not be dominated by it. Selection should be based on product features, premium and services provided.

6) Intermediaries should not rely on generic TOBA's but should ensure that they give accurate contract specific disclosures especially in the capacity in which they are acting and the services they provide;

7) The TOBA should include a section that makes clear that the customer is entitled to request information about commission;

8) Since a TOBA may be overlooked by a customer the guidance states that pertinent sections (such as services provided to the customer and rights of the customer about disclosure of commission) that may appear in the TOBA should also be included in, for example the quotation letter or as a separate short document.

Whilst the guidance is silent on the position of disclosure of total commission within chains (which is something that the FSA appeared to be quite keen on in its publications) the guidance provided by the ABI does state that there is no obligation on an intermediary to provide the

total amount of remuneration in the chain.

The FSA will be assessing whether commercial customers have benefited from clearer information in 2010/11. LIIBA has noted that if there is a negative response then this is likely to result in further action either directly by the FSA or via the European Commission.

Adequate protection of client assets and money

The FSA has sent a letter to all compliance officers reminding them of their firm's responsibilities under Principle 10:

'A firm must arrange adequate protection for clients' assets when it is responsible for them.'

It notes that in the current economic climate the protection of a client's entitlement is of paramount importance and firms 'should be paying due regard to the requirements we place on their systems and controls as outlined in CASS.'

This reminder has arisen as a result of a number of visits that the FSA conducted where it found that some firms failed to comply with basic CASS requirements. Firms need to recognise that whilst ongoing requirements may not provide protections as a going concern the rules are designed to minimize loss to clients upon insolvency. Senior management should be mindful of the following requirements:

1) Firms should have appropriate systems in place producing supporting documentation to comply with the CASS rules. Clear audit trails must be maintained particularly if firms operate a buffer in the client money account under CASS 5.5.10R;

2) Firms need to ensure that client money accounts should be opened up in accordance with the CASS rules. In particular there should be the appropriate exchange of letters with the bank and the title of the account must be sufficiently distinguishable from any other account that belongs to the firm;

3) Firms need to exercise due skill, care and diligence when selecting a bank where money is deposited. The FSA is reminding firms to document its due diligence. Senior management should consider the capital of the bank, the amount of client money placed and the credit rating of the bank.

The FSA will continue to visit firms in the second and third quarters of 2009 with a report on its findings being published in the fourth quarter.

Cross Border Business

Following extensive discussions between BIPAR, the European federation of Insurance Intermediaries, the European Commission and the Committee of European Insurance and Occupational Pension Supervisors (CEIOPs) agreement has been reached as to when intermediaries are deemed to be transacting cross border business ('Freedom of Services'). In such cases intermediaries need to advise the FSA who will make the necessary notification to the other Member State(s). The CEIOPs definition of Freedom of Services is based on an intermediary marketing, providing mediation services or actively seeking business from a client/consumer resident or established in another Member State.

This interpretation is contained in the Luxembourg Protocol which while not a legally binding instrument has been agreed by the supervisors of all Member States. The Protocol contains a 'non exhaustive' list of examples as to when an intermediary is conducting Freedom of Services:

1. The intermediary asks for and organises, on its own initiative meetings with clients established in another country.

2. Advertisements: the intermediary gives/sends information on specific products, conditions etc to selected groups of clients established in a given country/in specific languages of some EU MS etc. Here the advertisement has an active character, the intention of the intermediary to contact clients in another country is clear.

3. Electronic distance or distance marketing activities: if the content of the website of the intermediary is general and only in the language of the Member States of the intermediary, if it is not addressed to a specific group of clients or clients in specific countries, then the intermediary cannot be considered as actively seeking for these clients and therefore cannot be considered as having the intention to do Freedom of Services in the countries where those clients are established. If the intermediary is contacted by those clients it will not be considered as doing Freedom of Services in the countries of these clients.