

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

SECTION 1 – INTRODUCTION

- 1.1** The Financial Services Authority's (FSA) increased emphasis on disclosure, transparency and conflicts of interest management for firms doing business in the commercial insurance market along with its decision to set five outcomes to improve the experience of commercial customers when purchasing cover has prompted the development of this industry guidance.* It is designed to help insurance intermediaries achieve those outcomes and to comply with their legal obligations under the FSA's Principles for Businesses, applicable rules and guidance in the FSA *Handbook*, specifically ICOBS Chapter 4.

This guidance is only intended for dealings with *commercial customers*. The focus of this guidance is on providing customers with the requisite information to meet their needs when purchasing cover and to ensure that insurance intermediaries are managing appropriately any conflicts of interest that arise during the course of their business.

The FSA has reviewed this industry guidance** and has confirmed that it will take it into account when exercising its regulatory functions. This guidance is not mandatory and is not FSA guidance. This view cannot affect the rights of third parties.

The practical effect of this confirmation is that in the event of a breach of the relevant requirements, the FSA would take into account a firm's adherence to this guidance in any enforcement action.

DEPP 6.2.1 (4)(G)	The FSA will not take action against a person for <i>behaviour</i> that it considers to be in line with <i>guidance</i> , other materials published by the FSA in support of the <i>Handbook</i> or FSA-confirmed Industry Guidance which were current at the time of the <i>behaviour</i> in question.
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Should there be any conflict between this guidance and the FSA *Handbook*, the Handbook provisions will prevail.

* See FSA Feedback Statement 08/7 entitled *Transparency, disclosure and conflicts of interest in the commercial insurance market* from December 2008. The five outcomes are: (1) customers should have clear and comparable information about the commissions intermediaries receive; (2) customers should have clear and comparable information about the services intermediaries are providing; (3) customers should have clear information about the capacity in which an intermediary is acting; (4) customers should be alerted to their right to request commission; and 5) customers should be made aware where there is a chain of intermediaries.

** A more detailed explanation of the status and effect of FSA approved industry guidance can be found (at Annex 2) of PS07/16 http://www.fsa.gov.uk/pubs/policy/ps07_16.pdf).

This guidance provides firms with one approach to meet the relevant FSA requirements it does not represent the only means of achieving compliance. Firms which decide to adopt a different approach will not be presumed to be non compliant by the FSA.

This guidance is up to date as of [March 2009]. A condition of Industry Guidance status is that it will be revised in the light of any relevant changes to the FSA *Handbook*, statute or regulation. If you decide to follow this guidance it would be sensible to check whether there have been any such changes.

Definitions and abbreviations applicable to the Guidance

The following terms used in this guidance when shown in italics have the meaning ascribed to them in the FSA Glossary of terms:

- *Advise*
- *associate;*
- *behaviour;*
- *combined initial disclosure document;*
- *commercial customer;*
- *commission;*
- consumer;
- *contract of insurance;*
- *durable medium;*
- *financial promotion;*
- *firm;*
- *FSA*
- *guidance*
- *Handbook*
- *ICOBS;*
- *insurance intermediary;*

- *insurance undertaking*;
- *insurer*;
- *personal recommendation*
- *policyholder*
- *Principles*;
- *Renewal*; and
- *Rules*.

1.3 The FSA Handbook

Sections 1.4 to 1.8 of this Industry Guidance set out the key *Principles* and rules that this guidance has been developed to address and why they are relevant in the context of customer information needs and the management of conflicts of interest.

1.4 Principles for Businesses

The FSA's *Principles* for Businesses apply in whole or in part to every firm. They are a general statement of the fundamental obligations of firms under the regulatory system. Their status as rules means that the FSA may take action against firms that breach them.

Insurance intermediaries must observe all of the *Principles* for Businesses. However, the particular aims of this guidance are to help firms comply with Principles 1, 3, 6, 7 and 8, which relate to meeting the information needs of *commercial customers*, and the more effective management of conflicts of interest.

Principle 1 Integrity: a *firm* must conduct its business with integrity.

Principle 3 Management and control: a *firm* must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.

Principle 6 Customers' interests: a *firm* must pay due regard to the interests of its *customers* and treat them fairly.

Principle 7 Communications with clients: 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.

Principle 8 Conflicts of interest: a *firm* must manage conflicts of interest fairly, both between itself and its *customers* and between a *customer* and another *client*.

The application of Principles 6 and 7 are specific to a customer’s own particular circumstances and insurance intermediaries should take this into account when complying with them. For example, what is ‘fair’ when arranging insurance for a large commercial customer with a dedicated risk manager may be different from what is ‘fair’ to a smaller customer.

1.5 General Provisions

The General Provisions (GEN) of the *Handbook* apply to every firm. Every provision in the *Handbook* must be interpreted in the light of its purpose (GEN 2.2.1R). Any guidance given on the purpose of a provision is intended as an explanation to assist readers of the *Handbook*, but should not be taken as a complete or definitive explanation of a provision’s purpose.

1.6 Senior Management Arrangements, Systems and Controls (SYSC)

SYSC has several purposes including:

- (1) to encourage firms’ directors and senior managers to take appropriate practical responsibility for their firms’ arrangements on matters likely to be of interest to the FSA,
- (2) to increase certainty by amplifying Principle 3, and
- (3) to encourage firms to vest responsibility for effective and responsible organisation in specific directors and senior managers.

1.7 Prudential sourcebook for Mortgage and Home Finance Firms and Insurance Intermediaries (MIPRU)

When reading this guidance firms should bear in mind MIPRU 2.2.1R:

MIPRU 2.2.1R	A <i>firm</i> , other than a sole trader, must allocate the responsibility for the firm's <i>insurance mediation activity</i> to a director or senior manager.
MIPRU 2.2.3 (3) G	In the case of a <i>sole trader</i> , the sole trader will be responsible for the <i>firms’ insurance mediation activity</i> .

1.8 ICOBS

ICOBS sets out the rules and guidance governing how *insurance intermediaries* (and in some instances *insurers* also) should conduct their business with *commercial customers* or prospective commercial customers seeking insurance. ICOBS chapter 4 addresses information about the firm, its services and remuneration, also known as status disclosure. The relevant ICOBS *rules* together with the *guidance* supporting them are shown in boxed text where applicable.

SECTION 2 - INFORMATION NEEDS FOR COMMERCIAL CUSTOMERS

2.1 *ICOBS* Chapter 4 requires an *insurance intermediary* to make disclosure about the firm, its services and remuneration. *ICOBS* also contains wider information disclosure requirements which require that customers are provided with details about the product they are purchasing and a demands and needs statement. These disclosures must be made to *commercial customers* prior to the conclusion of an initial insurance contract and, if necessary, on its amendment or *renewal*, so that the customer can make an informed decision. Such further disclosure will be necessary if there has been any change in the status of, or services provided by, the insurance intermediary since the previous disclosure.

The FSA's research has shown that *commercial customers* are not well-informed about the services which are offered by firms, how firms are remunerated and what rights they have to require firms to provide information. Following this section's practical suggestions will help ensure that *commercial customers* are clear about the rights they have to obtain information from firms. This section also seeks to introduce a consistent approach which will assist commercial customers to understand how firms conduct their business and to make comparisons between different firms.

Model wordings to address the various disclosures required to fulfil Principle 7 and this guidance are to be found at Annexes 1 and 2. Firms are strongly recommended to use these model wordings unless they would not accurately represent the facts. Model wordings reduce the risk that firms will inadvertently breach the FSA's requirements. They also make it easier for commercial customers to understand the role and approach of one firm compared to another.

2.2 Breadth of search - Principles 6 and 7 and ICOBS

Customers should be adequately informed about the nature of the service that they can expect to receive from an *insurance intermediary* prior to entering into a contract with that intermediary. When providing this information, intermediaries should bear in mind ICOBS 2.2.2 R.

ICOBS 2.2.2 R	When a <i>firm</i> communicates information, including a <i>financial promotion</i> , to a <i>customer</i> or other <i>policyholder</i> , it must take reasonable steps to communicate it in a way that is clear, fair and not misleading.
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ICOBS 4.1.6R, ICOBS 4.1.7R and Principles 6 and 7 all contribute towards the customer's understanding about the services provided by their insurance intermediary.

ICOBS 4.1.6 R	(1) Prior to the conclusion of an initial <i>contract of insurance</i> and, if necessary, on its amendment or <i>renewal</i> , a <i>firm</i> must tell the <i>customer</i> whether:
	(a) it gives advice on the basis of a fair analysis of the market; or
	(b) it is under a contractual obligation to conduct <i>insurance mediation</i> business exclusively with one or more <i>insurance undertakings</i> ; or
	(c) it is not under a contractual obligation to conduct <i>insurance mediation</i> business exclusively with one or more <i>insurance undertakings</i> and does not give advice on the basis of a fair analysis of the market.
	(2) A <i>firm</i> that does not <i>advise</i> on the basis of a fair analysis of the market must inform its <i>customer</i> that he has the right to request the name of each <i>insurance undertaking</i> with which the <i>firm</i> may and does conduct business. A <i>firm</i> must comply with such a request.
ICOBS 4.1.7 R	Prior to conclusion of an initial <i>contract of insurance</i> with a <i>consumer</i> a <i>firm</i> must state whether it is giving a <i>personal recommendation</i> or information.

Insurance intermediaries which use a panel to make a fair analysis of the market should consider adopting the precautions set out in section 2.3 in order

to ensure that commercial customers have clear information about the services an intermediary provides, including the breadth of search they undertake.

An *insurance intermediary's* knowledge and expertise about a market may mean that they approach another insurance intermediary and use their services to access a particular product that is more suited to the needs of their *commercial customer*. The *commercial customer* should be informed when another *insurance intermediary* has been involved in the placing of their business.

An insurance intermediary may provide advice or information on a different basis to the same commercial customer in respect of different classes of insurance. For example, a fair analysis of the market may be conducted for liability insurance, but travel insurance may be offered from a single insurer. A firm may make an advised sale for one product and a non-advised sale for another. The status disclosure should make it clear to the commercial customer on what basis each type of insurance is being offered.

It is recommended that firms use the model template in Annex 2 when telling customers about the breadth of search offered to the customer, including when another intermediary has been used in placing their business.

2.3 Fair analysis and panels

ICOBs 4.1.8 G	(1) One way a <i>firm</i> may give advice on a fair analysis basis is by using 'panels' of <i>insurance undertakings</i> which are sufficient to enable the <i>firm</i> to give advice on a fair analysis basis and are reviewed regularly.
	(2) A <i>firm</i> which provides a service based on a fair analysis of the market (or from a sector of the market) should ensure that its analysis of the market and the available contracts is kept adequately up-to-date. For example, a <i>firm</i> should update its selection of contracts if aware that a contract has generally become available offering an improved product feature, or a better <i>premium</i> , compared with its current selection. The update frequency will depend on the extent to which new contracts are made available on the market.
	(3) The panel selection criteria will be important in determining whether the panel is sufficient to meet the 'fair analysis' criteria. Selection should be based on product features, <i>premiums</i> and services offered to <i>customers</i> , not solely on the benefit offered to the <i>firm</i> .

The selection of a panel should be based on a survey of the available products and criteria developed to ensure that they match the commercial customer’s needs as closely as possible. The criteria may include, but not be dominated by, the reward available to the *insurance intermediary*. If the product survey or criteria for selection are too narrow, the *insurance intermediary* may not claim that it has conducted a fair analysis. Once established, a panel requires vigilance to ensure that its members represent the best available selection of products in a particular class which the *insurance intermediary* can procure to meet the needs of the commercial customer.

Intermediaries claiming to have conducted a fair analysis of the market may wish to note the European Union’s Insurance Mediation Directive (IMD) (**Directive 2002/92/EC**). This interprets giving advice on the basis of a ‘fair analysis’ as an intermediary examining a ‘sufficiently large number of insurance contracts available on the market’, in order to determine whether the insurance recommended would be adequate to meet the customer’s needs.

Terms of Business Agreements (TOBAs)

There are a number of ways by which insurance intermediaries may meet the disclosure requirements in *ICOBS*. *ICOBS 4.5.1 G* suggests that a firm may wish to use the initial disclosure document. However, most firms have tended to use a TOBA as a vehicle for disclosure.

<i>ICOBS 4.5.1 G</i>	Using an initial disclosure document (see ICOBS 4 Annex 1G) or combined initial disclosure document satisfies the status disclosure, scope of service and fee disclosure requirements if it is used in accordance with its notes and provided to the customer at the correct time.
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While it is not compulsory for an *insurance intermediary* to have a written TOBA with a *commercial customer*, it is recommended that firms produce one. A TOBA is a convenient way to deliver many of the required disclosures, particularly since *ICOBS* mandates that certain information is given to the *commercial customer* in a *durable medium*.

This guidance recommends that a TOBA should set out all the terms of the contract between the *insurance intermediary* and the *commercial customer* whether those terms derive from general contract law, the law of agency or the requirements of the *FSA Handbook*.

However, intermediaries are reminded that the Rules require certain contract-specific disclosures to be given to the customer. Firms may not simply rely upon a generic TOBA but should ensure that they can and do give customers accurate contract-specific disclosures, especially in respect of the capacity in which they are acting, the breadth of searching of the market undertaken and

the services they provide to the customer. These disclosures are required prior to the conclusion of the contract.

Even the most clearly and comprehensively drawn up TOBA can be overlooked by the *commercial customer* during the sales process. To overcome this, and to ensure that the information forms a prominent part of the sales process, it is recommended that firms raise *commercial customers'* awareness by featuring pertinent sections of the TOBA, for example the intermediary's capacity or remuneration arrangements in a covering letter accompanying a quotation or in a separate, short document. Alternately, firms could reiterate certain information orally to the *commercial customer* (if the sale was made in that way).

Intermediaries should review whether the disclosure should be repeated when renewals are effected even if the TOBA itself does not need to change. The statements can be included on the invitation to renew.

Giving information in a TOBA may at times be impractical, for example when immediate cover is necessary. In such situations, the information may be provided orally to the customer, but should also be provided in a TOBA or other *durable medium* immediately thereafter conclusion of the contract.

2.4 How the intermediary is remunerated

In addition to Principles 1, 6 and 8, there are four provisions in ICOBS which are relevant to the disclosure of remuneration.

ICOBS 4.3.1 R	<p>(1) A firm must provide its <i>customer</i> with details of the amount of any <i>fees</i> other than <i>premium</i> monies for an <i>insurance mediation activity</i>.</p> <p>(2) The details must be given before the customer incurs liability to pay the <i>fee</i>, or before conclusion of the contract, whichever is earlier.</p> <p>(3) To the extent that an actual <i>fee</i> cannot be given, a <i>firm</i> must give the basis for calculation.</p>
ICOBS 4.4.1 R	<p>(1) An <i>insurance intermediary</i> must, on a <i>commercial customer's</i> request, promptly disclose the <i>commission</i> that it and any <i>associate</i> receives in connection with a <i>policy</i>.</p>
	<p>(2) Disclosure must be in cash terms (estimated, if necessary) and in writing or another <i>durable medium</i>. To the extent this is not possible, the <i>firm</i> must give the basis</p>

	for calculation.
ICOBS 4.4.2 G	An <i>insurance intermediary</i> should include all forms of remuneration from any arrangements it may have. This includes arrangements for sharing profits, for payments relating to the volume of sales, and for payments from premium finance companies in connection with arranging finance.
ICOBS 4.4.3 G	1) The commission disclosure <i>rule</i> is additional to the general law on the fiduciary obligations of an agent in that it applies whether or not the <i>insurance intermediary</i> is an agent of the <i>commercial customer</i> .
	(2) In relation to <i>contracts of insurance</i> , the essence of these fiduciary obligations is generally a duty to account to the agent's principal. But where a <i>customer</i> employs an <i>insurance intermediary</i> by way of business and does not remunerate him, and where it is usual for the <i>firm</i> to be remunerated by way of <i>commission</i> paid by the <i>insurer</i> out of premium payable by the <i>customer</i> , then there is no duty to account but if the <i>customer</i> asks what the <i>firm's</i> remuneration is, it must tell him.

Firms should bear in mind that the FSA's definition of an *associate* extends to affiliated companies and appointed representatives. A full definition of an *associate* can be found in the FSA's Glossary.

Disclosure of remuneration

Intermediaries must have in place policies, written procedure(s) and systems to be able to disclose commission on-request. The procedures by which this system operates must be clearly communicated to all relevant staff. There must also be in place systems that identify the functions which the intermediary performs on behalf of the *insurer* or any other party with whom it has a commercial relationship in return for the commission received from that source.

It is recommended that firms use simple language to help *commercial customers* understand the potential value to the firm of contingent arrangements (volume, profit etc). The following wording may help:

As you can see, this arrangement is based upon volume / performance criteria during this year and so the value of the arrangement to us cannot be accurately calculated today. However, should our account achieve the income and profit targets set by the insurer, the maximum extra commission we could

earn is x%. This could mean us earning up to a maximum extra commission in respect of your policy of £x.”

Clearly firms will need to calculate the value of each arrangement should they choose to use this approach.

To meet *commercial customers'* information needs it is important that the information is presented in a clear way. Where the disclosure is to be made in writing, it is recommended that firms use the template set out in Annex one so as to facilitate the uniformity of the disclosure.

The commercial customer's right to ask

It is recommended that intermediaries, at regular intervals and in writing, make a plain and clear statement to the *commercial customer* about remuneration so that *the commercial customer* readily understands that they are entitled to request information regarding any commission which the intermediary may have received as a result of placing the commercial customer's insurances. The following wording is suggested:

“In good time before the conclusion of each insurance contract, or upon renewal, we will remind you of your right to be informed of the level of commission which we receive from underwriters.

You are entitled, at any time, to request information regarding any commission which we may have received as a result of placing your insurance business.”

We suggest that the interval between statements should not be longer than twelve months. The statements should be made in either:

- the covering letter that might accompany a written quotation;
- a document of no more than one page in length; or
- orally.

Oral disclosure

There may be circumstances where using a written statement to communicate the right to ask would not be possible before the contract was concluded e.g. telesales. In such circumstances, firms should make an oral disclosure and then repeat the disclosure in writing in its post-sale communication with the commercial customer. Where an oral disclosure is made, the firm should ensure that an appropriate file note of the conversation is made and kept.

**SECTION 3 – CAPACITY AND CONFLICTS OF INTEREST –
PRINCIPLE 8**

This section provides guidance on how a firm can meet its obligations under Principles 3 and 8 and with the requirements of SYSC. These require an *insurance intermediary* to address actual and potential conflicts of interest arising within its business.

SYSC 10.1.3 R	A <i>firm</i> must take all reasonable steps to identify conflicts of interest between:
	(1) the <i>firm</i> , including its managers, employees, <i>appointed representatives</i> (or, where applicable, <i>tied agents</i>), or any <i>person</i> directly or indirectly linked to them by <i>control</i> , and a <i>client</i> of the <i>firm</i> ; or
	2) one <i>client</i> of the <i>firm</i> and another <i>client</i> ; that arise or may arise in the course of the <i>firm</i> providing any service referred to in SYSC 10.1.1R.
SYSC 10.1.4 R	For the purposes of identifying the types of conflict of interest that arise, or may arise, in the course of providing a service and whose existence may entail a material risk of damage to the interests of a client, a common platform firm must take into account, as a minimum, whether the firm or a relevant person, or a person directly or indirectly linked by control to the firm: (1) is likely to make a financial gain, or avoid a financial loss, at the expense of the client; (2) has an interest in the outcome of a service provided to the client or of a transaction carried out on behalf of the client, which is distinct from the client's interest in that outcome; (3) has a financial or other incentive to favour the interest of another client or group of clients over the interests of the client;

	<p>(4) carries on the same business as the client; or</p> <p>(5) receives or will receive from a person other than the client an inducement in relation to a service provided to the client, in the form of monies, goods or services, other than the standard commission or fee for that service.</p> <p>The conflict of interest may result from the firm or person providing a service referred to in SYSC 10.1.1 R or engaging in any other activity.</p>
SYSC 10.1.4 A G	Other <i>firms</i> should take account of the <i>rule</i> on the types of conflicts (see SYSC 10.1.4R) as if it were <i>guidance</i> (and as if “should” appeared in that rule instead of “must”) as explained in SYSC 1 Annex 1.3.3R, except when they produce or arrange the production of <i>investment research</i> in accordance with COBS 12.2, or produce or disseminate <i>non-independent research</i> in accordance with COBS 12.3 (see SYSC 10.1.16R).

3.1 An *insurance intermediary* faces a conflict of interest where:

- the firm’s own interests conflict with those of a *commercial customer*; or
- the firm is unable to act in the best interests of one *commercial customer* without adversely affecting the interests of another *commercial customer*.

Intermediaries should consider whether a relationship with a party other than the *commercial customer* has influenced the advice to the commercial customer in arranging insurance or the selection of the *insurer*.

It is the duty of an *insurance intermediary* to manage conflicts of interest so that the intermediary’s interest does not conflict with the interests of *commercial customers* and of any insurers on whose behalf they may act. In this way the *insurance intermediary* will ensure that conflicts of interest arising from remuneration arrangements or business models are properly disclosed and managed. An *insurance intermediary* may manage such conflicts either by disclosure or withdrawal from the engagement.

An *insurance intermediary* must decline to act for the commercial customer unless in the particular circumstances of the case, disclosure and informed consent are sufficient to resolve the conflict.

The FSA has given additional guidance on the circumstances which may give rise to a conflict of interest in SYSC 10.1.5 R.

Conflicts policy and management

In order to comply with Principles 3 and 8 and with the requirements of SYSC, an *insurance intermediary* must address actual and potential conflicts of interest arising within its business.

SYSC 3.1.1 R	A <i>firm</i> must take reasonable care to establish and maintain such systems and controls as are appropriate to its business.
SYSC 10.1.7 R	A <i>firm</i> must maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps to prevent conflicts of interest as defined in SYSC 10.1.3R from constituting or giving rise to a material risk of damage to the interests of its <i>clients</i> .
SYSC 10.1.8 R	(1) If arrangements made by a <i>firm</i> under SYSC 10.1.7R to manage conflicts of interest are not sufficient to ensure, with reasonable confidence, that risks of damage to the interests of a <i>client</i> will be prevented, the <i>firm</i> must clearly disclose the general nature and/or sources of conflicts of interest to the <i>client</i> before undertaking business for the <i>client</i> .
	(2) The disclosure must:
	(a)
	(b) include sufficient detail, taking into account the nature of the <i>client</i> , to enable that <i>client</i> to take an informed decision with respect to the service in the context of which the conflict of interest arises.
SYSC 10.1.9 G	<i>Firms</i> should aim to identify and manage the conflicts of interest arising in relation to their various business lines and their <i>group's</i> activities under a comprehensive <i>conflicts of interest policy</i> . In particular, the disclosure of conflicts of interest by a <i>firm</i> should not exempt it from the obligation to maintain and operate the effective organisational and administrative arrangements under SYSC 10.1.7R. While disclosure of specific conflicts of interest is required by SYSC 10.1.8R, an over-reliance on disclosure without adequate consideration as to how conflicts may appropriately be managed is not permitted.

To help manage conflicts of interest, *insurance intermediaries* should have a conflicts of interest policy which is approved and regularly reviewed by the

governing body of the *firm* and which is monitored by the compliance or other officer of the firm.

As a first step it is important to conduct a thorough risk assessment of the firm's business to identify those activities that have the potential to give rise to conflicts of interest and to assess the risk of such conflicts actually arising and adversely affecting *commercial customers*. This assessment will enable firms to determine what control systems should be in place to identify and manage the risks and to a determination of who within the management team is responsible for ensuring that the control systems operate effectively and are regularly reviewed and tested.

Intermediaries should be able to demonstrate that they have examined their corporate governance, internal procedures and individual senior management systems and controls to ensure that conflicts of interest are identified and appropriately managed. It is not sufficient to have informal management processes and controls to deal with potential conflicts of interest.

Two letters have been sent by the FSA to Chief Executives (on 18th November, 2005 and 6th December, 2006) which make particular reference to some of the issues which intermediaries might need to consider, and all intermediaries should be familiar with these. These letters can be viewed by accessing the links below:

http://www.fsa.gov.uk/pubs/ceo/conflicts_18nov05.pdf
http://www.fsa.gov.uk/pubs/ceo/commission_disclosure.pdf

To avoid a conflict of interest altogether, an intermediary should not enter into an engagement with any other party to a transaction where the intermediary already acts for a *commercial customer* in relation to that transaction. Such a course may not be practicable where the intermediary already has an agency relationship with an *insurer* and the *commercial customer* is to be offered insurance from that insurer. In such circumstances, the intermediary should disclose to the *commercial customer*, in general terms and before the insurance is arranged, the identity and interest of the other party, in this example the *insurer*. In addition, the intermediary should, on request, disclose any commission received as a direct or indirect result of entering into the transaction.

A firm should have conflict management controls which:

- are carefully thought through and benchmarked against the sector;
- form an integral part of your overall risk management reviews and be regularly monitored by the executive;

- are based on robust, up-to-date advice and well documented;
- supported by an adequate compliance system;
- regularly reviewed by senior management; and
- owned by a particular member of the board.

Under the provisions of SYSC, management control systems, reporting procedures and corporate governance practices need to demonstrate that the management of conflicts is a live and ongoing activity within the business and one that is championed by senior management and at board level. For instance, one way of demonstrating this would be to have conflict management as a standing agenda item at board meetings.

3.2 Circumstances in which conflicts of interest may arise

There are various circumstances in which an insurance intermediary might encounter a conflict of interest, whether or not related to remuneration. Examples include:

- profit shares: where remuneration is based on the profitability of business placed with an insurer;
- volume over-riders: where remuneration is based on the volume of business placed with an insurer;
- corporate hospitality and gifts: which could amount to inducements;
- claims handling and binding authorities: where the intermediary would not be able to act in the best interests of both client and insurer, especially in the circumstances of a contested claim;
- training support: which could amount to an inducement if provided by an insurer;
- soft loans: where an insurer might seek to induce the placement of business by offering credit at below market terms;
- reinsurance conflicts: where placement of business is used to encourage insurers to use the intermediary to arrange reinsurance contracts;
- contingent commissions: where payment of an enhanced commission depends upon the intermediary procuring an outcome favourable to the insurer; and

- work transfer: where the intermediary received additional and possibly enhanced remuneration for the provision of specified services to an insurer.

Firms should consider carefully how to manage circumstances such as those listed above.

Internal controls

Insurance intermediaries need to be able to demonstrate that they have in place rigorous internal controls for identifying and managing potential conflicts of interest and a mechanism for preventing them adversely affecting the firm's commercial customers. Once in place, these controls, and the policies and procedures which they support, need to be regularly tested, reviewed and updated and there must be evidence that staff have been properly trained to follow them.

For example, intermediaries will need to be able to demonstrate that:

- the firm has undertaken adequate risk assessments and created/updated a conflict management policy for the business;
- the firm's senior management promotes the core values of treating customers fairly and a culture within the business that is focused on mitigating or removing potential conflicts of interest;
- the firm's conflict management policy has been properly promoted at all levels within the business;
- the firm has control systems in place to ensure that the conflict management policy is observed within the business;
- the firm collects management information and monitors key performance indicators to ensure that the control systems are effective; and
- the firm has invested in adequate staff and management training to promote change within the business.

3.3 Capacity - Principles 6, 7 and 8

One way to help manage conflicts of interest that arise from commercial relationships is to give the *commercial customer* clear information about the capacity in which an *insurance intermediary* is acting – i.e. whether it is acting for them, for the *insurer* or, in some cases, for both.

A *commercial customer* should have clear information about the capacity in which an insurance intermediary is acting – i.e. whether it is acting for them, for the insurer or, in some cases, for both. This information needs to be given in good time before the commercial customer enters into a contract.

It is important that intermediaries ensure that they use clear descriptions about their capacity when communicating with *commercial customers*. To facilitate this, and to ensure that this information is given prominence in the sales process, it is recommended that firms use the template set out in Annex 2.

Many intermediaries have agency relationships with both their *commercial customers* and one or more *insurers*. They will owe the fiduciary duties of an agent to both parties to an insurance transaction. In such situations the intermediary must take care to manage the conflicts that may arise. Further explanations of such conflicts and guidance as to how they should be addressed are set out in section 3.1.

Where an insurance intermediary makes a disclosure about the capacity in which it is acting (i.e. whether for the commercial customer alone, for the insurer, or for both), generic statements used in a TOBA would not be sufficient – intermediaries must ensure that each customer receives the correct disclosure specific to their individual circumstances.

Annex 1

Our Earnings

As your chosen insurance intermediary, we earn income in two separate ways.

1. We can earn by charging you a fee for our service. Whenever we charge a fee, that amount will be agreed with you in advance and will be disclosed to you separately to the insurance premium. If we have charged you a fee, this information will have been provided to you already alongside details of the premium.
2. We can earn by receiving a commission payment from the insurance company with which the insurance is placed. This amount will usually be calculated as a percentage of the insurance premium and the percentage will have been contractually agreed with the insurance company. We earn different percentages for different classes of business and from different insurance companies.

The table below sets out details of the commission and any other income we might earn in respect of handling your insurance.

	£
Direct earnings	
1) Commission – we earn the following:	
2) Premium finance – for arranging the funding of your insurance premium, we will earn:	
Possible additional earnings	
1) Profit share agreement - we have an agreement with [insurer name] that if our account with them meets certain pre-agreed volume and profit targets during this year, we will receive an additional payment from them. The value of the arrangement to us cannot be accurately calculated today. However, should our account achieve the income and profit targets set by the insurer, the maximum extra commission we could earn is x%. This could mean us earning up to a maximum extra commission in respect of your policy of £x. If you would like further details on the precise method of calculation of this agreement, please contact [insert name].	
2) Volume commission over ride - we have an agreement with [insurer name] that if our account with them meets certain pre-agreed volume targets during this year, we will receive an additional payment from them. The value of the arrangement to us cannot be accurately calculated today. However, should	

<p>our account achieve the income targets set by the insurer, the maximum extra commission we could earn is x%. This could mean us earning up to a maximum extra commission in respect of your policy of £x.</p>	
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<p>If you would like further details on the precise method of calculation of this agreement, please contact [insert name].</p>	
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Our capacity and services

Important information

The following information is in relation to the [enter the contract-specific name] insurance you have asked us to arrange.

The capacity in which we are acting

Sourcing a suitable policy	We act as your agent	
	We act as agent of the insurer	
Placing the insurance	We act as your agent	
	We act as agent of the insurer	
In the event of a claim	We will act as your agent	
	We will act as agent of the insurer	

How we made our selection

We have carried out ‘fair analysis’ of the market in order to identify a suitable product. This means that we have compared products from a sufficiently large range of insurance providers in terms of cover, price, quality of service and other relevant features in order to select appropriate policies for you.	
Our search for a product to meet your requirements has involved a limited number of insurers. We would be happy to discuss with you the scope and outcome of our search. You can ask us, at any time, for a list of the insurers we use.	
To access the insurance product that most suits your needs, we will use another intermediary to help place your business.	
We only offer cover from a single insurer, XYZ Insurance Company Limited in respect of this type of insurance.	

Our remuneration

You are entitled, at any time, to request information regarding any commission which we may have received as a result of placing your insurance business.