

## 2.4. Theme 4: Short-term insurance

This theme focusses on those RDR proposals impacting on the distribution of short-term insurance policies. The theme covers proposals relating to adviser remuneration in relation to these products. It also deals with proposals on outsourcing arrangements between advisers and short-term insurers, including specific proposals relating to insurance premium collection, issuing of policy documents and binder agreements. Note that although the proposals on binder agreements are dealt with under this theme because they are most common in the short-term insurance environment, these proposals are also relevant in the long-term insurance space. The theme also covers proposals in respect of short-term insurance cover cancellations.

### 2.4.1. Key stakeholder feedback and initial responses for Theme 4

#### *(a) Ongoing product servicing:*

In response to Proposal E, relating to standards for ongoing product servicing, similar concerns were raised by short-term insurance stakeholders to those summarised above in Theme 3 relating to long-term insurance. As was the case for the long-term insurance sector, commentators highlighted that it would be important to identify the particular types of post-sale servicing activities envisaged. Although it was generally recognised that post-sale servicing interactions are more frequent for short-term policies than for long-term policies, clarity was still requested on the regulator's expectations as to which types of post-sale services would entitle an adviser to ongoing service fees.

#### *(b) Short-term insurance remuneration model:*

Next steps for Proposal UU, namely the proposed remuneration model for selling and servicing short-term insurance policies, were largely discussed in the RDR Phase 1 Status Update, focusing on the repeal and replacement of the current "section 8(5) fee" permitted by the Short-term Insurance Act. In addition, further technical work will take place in the course of 2016 to test the impacts of different commission cap levels for different levels and types of adviser sales activity and different product combinations.

As pointed out in the RDR Phase 1 Status Update, this consultation will include discussion on whether the remuneration payable by short-term insurers in respect of post-sale

servicing, and the remuneration payable by them for the actual product sale (both payable as-and-when premiums are received) should be subject to separate standards and caps, or whether they should both be addressed through a single cap on commission. We have mentioned in the RDR Phase 1 Status Update however that, despite the simplicity and ease of implementing a single commission cap, this approach does not enable appropriate reward for advisers who provide ongoing services as opposed to those who do not. As for the long-term insurance remuneration model, we would therefore like to pursue an appropriate link between the entitlement to as-and-when remuneration and at least some degree of ongoing service.

*(c) Premium collection:*

Short-term insurance commentators expressed mixed views on the proposal that the outsourcing of premium collection should be limited to qualifying intermediaries (Proposal F). Some commentators proposed that premium collection by financial advisers should be prohibited completely, while others felt that this was a useful service and that sufficient safeguards were in place to mitigate risks of misconduct. A number of commentators proposed that premium collection should be carved out of the scope of "intermediary services" (as currently defined in the FAIS Act) and instead be regarded as an outsourced service on behalf of the insurer for RDR purposes. The FSB is considering the implications of this approach as part of the broader review of the RDR proposals relating to outsourcing, which we discussed in the RDR Phase 1 Status Update. It was also pointed out that premium collection may be necessary in the case of non-traditional bundled products such as travel insurance or credit insurance, where the premium is collected together with payment for the primary transaction.

The FSB intends to proceed with Proposal F regarding standards for premium collection, and consultation with the industry reference groups for both long-term risk and short-term insurance will take place regarding who should be a "qualifying intermediary" and the standards for such intermediaries. Consultation will include discussion on the circumstances in which intermediaries in so-called non-traditional insurance markets could be permitted to collect insurance premiums.

*(d) RDR application to commercial lines business:*

A general concern raised was that the RDR discussion document is not clear on the extent to which the various proposals will apply to commercial lines business. This point is well

made and the FSB will engage with the short-term insurance industry reference group to consider the extent to which the various RDR proposals are relevant to, and impact on, the distribution of commercial lines policies. In particular, note that we indicated in the RDR Phase 1 Status Update that we are considering the extent to which commercial lines advisers should be permitted to enter into binder arrangements.

#### **2.4.2. Implementation phases for Theme 4**

##### ***(a) Phase 1***

As discussed in the RDR Phase 1 Status Update, the following proposals relevant to this theme fall within Phase 1 and next steps for these proposals are set out in that document:

- *Proposals J<sup>18</sup>, Z and AA*: Proposals relating to standards for outsourced services and restricted outsourcing to financial advisers.
- *Proposal UU*: Remuneration for selling and servicing short-term insurance policies (to the extent dealt with in the RDR Phase 1 Status Update in relation to the removal of the "section 8(5) fee").
- *Proposal VV*: Conditions for short-term insurance cover cancellations.
- *Proposal ZZ*: Binder fees payable for multi-tied intermediaries to be capped.
- *Proposal BBB*: Outsourcing fees for issuing insurance policy documents (the RDR Phase 1 Status Update advised that the FSB does not intend to proceed with this proposal).

##### ***(b) Phase 2***

Implementation of the future commission levels for short-term insurance policies will take place in this Phase. Consideration will be given to phasing the expected reduction of commission caps in over a period of two to three years, subject to the outcome of technical impact testing. The final commission model will also reflect the outcome of consultations regarding how best, if at all, to distinguish between remuneration for selling the policy and remuneration for on-going servicing.

It follows that standards in relation to advice fees and the requirement for short-term insurers to facilitate advice fees (Proposals JJ, KK and LL) will also need to be

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<sup>18</sup>Although not explicitly identified as a Phase 1 proposal, Proposal J is closely linked with Proposals Z and AA.

implemented in Phase 2, with due allowance for lead times for product suppliers to effect any necessary system changes.<sup>19</sup>

The FSB also intends to implement Proposal F, restricting premium collection to qualifying intermediaries, in Phase 2.

***(c) Phase 3***

Any refinement of the short-term remuneration model that may be required to align with the final adviser categorisation model would be implemented during this phase.

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<sup>19</sup> It is however the FSB's understanding that most short-term insurers already have systems in place for the payment of section 8(5) fees, which systems should be reasonably capable of being adapted for the facilitation of advice fees.