

Insurance Distribution Directive (IDD)

ARE YOU READY?



What is the Insurance Distribution Directive?

The Insurance Distribution Directive or IDD for short is the new European Union directive covering the sale and advice of insurance products. It is mainly focused on the general insurance profession. This replaces the Insurance Mediation Directive which was published on 14 January 2003 and formed the basis of general insurance regulations by the FSA, which came into effect in the UK on 14 January 2005.

So here we are some 14 years later, and the world has moved on somewhat and it was felt that the regulatory landscape needed to be updated to reflect current requirements.

It also built on the experiences gathered over the years and updated the language as well as the rules. Hence in part why it is such a big undertaking.

1 When does it start to affect the UK insurance broking profession?

EU countries are required to transpose IDD into national law by 1 July 2018. However the European Commission has pushed back the application date until 1 October 2018.

2 What are its main aims?

As well as bringing the regulations up to date, it also aims to create more of a level playing field between the various providers of insurance whether producers or distributors.

3

Who does it affect?

It affects everybody within the general insurance sector, insurers, wholesalers, MGA's and insurance brokers and intermediaries whether or not insurance is their full-time role. For those secondary markets where insurance is not full time, (such as motor traders, retailers and travel agents for example) we will see a significant increase in regulation to bring them more fully into the regulatory perimeter and improve customer protection, which after all is one of the FCA's main objectives. The Secondary market is now retitled "Ancillary Insurance Intermediaries" or All.

4

What has the FCA done so far?

The FCA had split the topic into three, which means that we have seen three different consultation papers which set out the FCA's proposals.

The first set out the main changes which will impact on the day to day processes, the second looked broadly at the Insurance Product Information Document or IPID (a replacement for Key Facts within general insurance, and only for consumers (i.e. domestic customers) therefore excludes commercial customers) and the third covered remaining matters such as conflicts.

The FCA has now issued all three Policy statements from the first major consultation.

5

What are the main areas to consider?

Employee Knowledge & Competence

The IDD introduces a requirement for a minimum 15 hours per annum of Continuing Professional Development (CPD). The CPD year is not mandated by the regulator and firms will need to adapt this into their existing T&C Requirements. This is NOT in addition to any current company or professional body requirement.

The form and content of the CPD can be adapted according to the nature and complexity of an employee's role and the FCA does not specify any particular mix of Structured or Unstructured CPD, it is for each firm to decide.

For general insurance contracts, a firm must, including in relation to the relevant employee, demonstrate compliance with eight professional knowledge and competence requirements.

The CPD requirement applies to employees who are either directly involved in the carrying out of the firm's insurance distribution activities, those responsible for the supervision of such employees and those within the management structure with responsibility for the firm's insurance distribution activities.

Professional Indemnity Insurance

The IDD requires that all intermediaries have in place professional indemnity insurance or a comparable guarantee with minimum levels of cover of €1,250,000 per claim per year, and €1,850,000 per year in aggregate for all claims.

The minimums are not a recommendation or advice from the regulator as to what is needed and it is for each firm to determine what level of PI cover is needed to meet its own specific circumstances.

Complaints

Regulated firms must have in place a procedure for dealing with a complaint from any customer, not just those eligible to use the Financial Ombudsman Service (FOS) (although the scope of FOS remains unchanged).

Conduct of Business

The IDD introduces general principles that apply to all insurance distributors. These are overarching requirements, which apply in a similar way to the current FCA 'Principles for Businesses'.

In summary, the IDD general principles say that:

1. firms must act honestly, fairly and professionally in accordance with their customers' best interests (The Best Interest Rule)
2. firms must communicate in a way which is clear, fair and not misleading. Marketing materials must be clearly identifiable as such
3. remuneration of a firm or its employees, and performance management of employees, must not conflict with the duty to act in accordance with their customers' best interests.

Therefore, a new rule will be introduced in ICOBS to cater for the first point. This will also be extended to apply to wholesalers. In ICOBS, 'customer' is defined as being a policyholder or prospective policyholder. This definition applies to the new customers' best interests rule.

The Current ICOBS rules on Financial Promotions will be amended to include the second point ensuring that marketing material is clearly identifiable as such and there will be a new rule in SYSC to reinforce principle 3.

Pre Contract Disclosure

In summary, these include:

- firms must disclose whether they are an insurer or an intermediary
- firms must disclose whether they provide advice
- intermediaries must disclose whether they act for the customer or the insurer.

This material is included in many Client Terms of Business used by Insurance Brokers.

Insurance Brokers must state, where they give advice, that it is based on a personal recommendation and if a fair and personal analysis of the market has been used, as opposed to the current requirement which states a "fair analysis".

Conflicts of Interest

In summary, the changes say that:

- intermediaries must make disclosures about shareholding links between the intermediary and any insurers. This applies to any shareholding of 10% or more.
- where intermediaries do not provide advice based on a fair and personal analysis of the market, and use a Panel, they must disclose the names of insurers on that panel with whom they may place business, this must be disclosed up front, not on request as is the current rule.
- intermediaries must disclose the nature of their remuneration in relation to the insurance contract and whether they work based on a fee, commission. This is applicable to all customers, not just commercial.
- all firms must disclose fees payable by the customer in cash terms. This includes fees which may become payable (such as for mid-term adjustments).

Means of Providing Information

The FCA will introduce a new section in ICOBS 4 setting out new requirements for Providing Information.

At renewal, firms can use existing distribution methods, but must give the customer the choice to receive the documents by other means.

Non Advised Sales

A new rule requiring that all products offered must be consistent with the customer's demands and needs. A firm cannot just provide a generic statement of demands and needs without some matching of an individual customer's needs to the products offered. However, the FCA do not expect non-advised sales to go beyond the customer's high-level demands and needs. This is very similar to the current position.

Advised Sales

A new rule requires firms to provide the customer with a personalised recommendation explaining why the recommended product would best meet the customer's needs and a requirement to act in the **customer's best interests**, if the firm does not offer a product which meets the customer's needs it should say so.

This includes any needs that have not been met being highlighted. Again, like the current position.

Cross Selling and Ancillary Insurance Intermediaries (All) (e.g. Car dealers and so on)

The IDD introduces major changes in both these areas and all brokers should ensure they understand how these may affect their business.

Connected Travel Insurance (CTI) Providers.

The IDD will extend the minimum PII levels and the requirement for employees to undertake 15 hours of CPD per year to CTI providers.

The regime for out-of-scope Alls

These are firms who are outside the UK regulatory perimeter by virtue of the Connected Contracts Exclusion (CCE). Common examples include electronic goods and furniture retailers. (See - <https://www.handbook.fca.org.uk/handbook/glossary/G1364.html>)

In short, a short-term contract with a premium of €500 or less and covers very specific risks such as breakdown, loss of, or damage to, non-motor goods supplied by the provider. The link above gives the full definition.



The IDD introduces requirements which apply to out-of-scope AIs. Responsibility for ensuring an out-of-scope AI complies with these requirements sits with the authorised firm (insurer or intermediary) which uses the AI to distribute their products

6 Will the insurance brokers have much to do?

Potentially yes. All processes and documentation will need to be reviewed to ensure it reflects the new language and requirements.

There will be a big change in T&C with the need to provide more evidence in more topics and of course mandatory CPD.

Also, how will they manage the new (albeit soft) disclosure of earnings for all clients?

There are a number of other changes which Insurance Brokers need to take account of which are outlined in the Policy Statements.

7 If it's an EU piece of legislation and we are leaving the EU, should we bother?

Of course we should. We will still be EU members at the 1 October 2018 and the government has given a commitment to enshrine EU directives into UK law.

8 What can be done when we still do not know all the rules?

It will be a challenge, and that is why firms need to look at this now and look perhaps at a common-sense approach.

The bulk of the rules are pretty well there so brokers should be working to implement these.

As for the remainder, much will already be in place given the FSA's penchant for gold plating, and strangely enough, we now see the benefit of this as much in all three elements was already in place in the UK, as we have a much stronger regulatory regime.

The Insurance Distribution Directive – Update

On 2 February the European Commission announced they will not implement the Directive until 1 October 2018.

This was agreed by both the European Council and the European Parliament.

The announcement can be viewed at – <https://www.gov.uk/government/consultations/transposition-of-the-insurance-distribution-directive>

Firms should still be working towards implementation of all the required changes, but this additional period will give all parties more time to ensure that they are fully prepared.

Don't be afraid to seek expert external help that can ensure you have correctly understood the key issues and have/are taking the right action to bring your business into line with the new IDD requirements.



John Miller, Head of London Business, RWA Business Consultancy

John has more than 30 years' experience in the world of general insurance, working for some of the largest UK brands including Norwich Union and Aviva. His experience includes mergers and acquisitions, business development, marketing and propositions. At RWA John has responsibility for developing the business in London in addition to managing the relationship with several key clients.

