Insurance Intermediation

January 2023

bipar

The European Federation of Insurance Intermediaries

Avenue Albert-Elisabeth 40
1200 Brussels - Belgium
Tel : +32-2-735.60.48
bipar@bipar.eu - www.bipar.eu

Table of contents

Executive summary

The purpose of the present document is to highlight the contribution made by insurance intermediaries to the well-functioning of the European insurance market and the value they offer to insurance buyers and insurers.

Insurance intermediation: a dynamic, innovative and competitive sector

The large majority of the 800,000 insurance intermediaries in the EU are micro and SME scale undertakings with a local focus. They have an in-depth knowledge of their local clients and the tailor-made products and services they offer. There are also a number of global and multinational business insurance intermediaries and major medium-sized domestic intermediaries.

Insurance intermediaries in the majority of Member States intermediate in over 50% of the non-life insurance premiums. For life insurance, the market share is generally lower, and the situation is more varied.

Consumers and insurers have the choice to use intermediaries or not. Without the appreciation of the client for the added value offered by his or her intermediary, the client would go elsewhere in a highly competitive market. Intermediaries only exist because they are relevant.

What do intermediaries do?

Intermediaries play a key role in the insurance process.

For clients, intermediaries:
- identify the risks clients face;
- ensure that clients take informed decisions about the risks they wish to insure;
- design new and innovative solutions;
- reduce the clients' search costs;
- put their knowledge at the service of the clients;
- assist their clients with claims related services and policy administration services.

For insurers, intermediaries:
- perform services with no fixed costs which insurers would otherwise have to perform themselves;
- facilitate entry into the market by new insurance companies, as the latter can reach a wide client base without having to incur the costs of building a distribution network;
- intermediaries assist insurers with claims-related services and policy administration services.

How do intermediaries help clients in the choice of a particular insurance?

Once the risks of the client are identified and the insurance needs are defined, there are several factors determining the recommendation that intermediaries make to their clients when advising them on the choice of a particular insurance or insurer.

Apart from the price, these factors include, inter alia:
- the breadth of coverage available (capacity),
- the insurer's flexibility in agreeing coverage,
- the insurer's image and reputation, especially in respect of claims service (speed, fairness of settlements, additional benefits to claimants),
- the quality and clarity of documentation provided,
- the insurer's speed in issuing documentation or in quoting terms,
- timeliness in inviting renewal,
- the technical competence of the insurer's staff,
- the quality of the other services provided by the insurer, his locational proximity.

Price is not the only determining factor in the choice of insurance.

How are insurance intermediaries paid?

Clients have the choice of two primary mechanisms by which insurance intermediaries are compensated for their services:

- A **fee** system under which the client pays directly for the services provided;
- A **commission** system under which the intermediary is paid a percentage of the premium paid by the client for coverage based upon the intermediary's agreement with the carrier.

Many insurance intermediaries offer the choice to the client (particularly in the business segment) to work either on a commission or a fee basis. When considering the choice between the two, a number of factors need to be considered by both the intermediary and the client in their dialogue. For example: commission is only payable if a contract ensues. In a fee system, clients should consider if they will be able to afford to pay fees based on time spent in the event of a claim. The commission system satisfies a need for services in the future. In any event, it is the client who has the choice of the remuneration system that best suits his requirements as there is no compulsion to avail of the service of any insurance intermediary.

The transparent coexistence of various remuneration systems is the best guarantee for competitive and dynamic markets (more info about remuneration below).

The remuneration of the intermediary, being in principle commission-based with the possibility to agree fees, has been a major contributing factor to the successful and competitive development of insurance markets all over the world. The decision to work on a fee or commission basis is a decision that should be taken between the parties based upon a transparent dialogue on the various options.

From a more macro-socio-economic perspective

Insurance intermediaries:

- take an active part in the Single market: they allow insurers/producers to offer services in different Member States and consumers to access insurance services throughout Europe;
- are catalysts for greater competition in the insurance and financial sectors and are encouraging all players to offer innovative and competitive products and services;
- work within a European regulatory framework that protects consumers. A very large number of texts, in particular the Directive on Insurance Distribution (IDD) and on Markets in Financial Instruments (MiFID) apply and make it possible to reinforce transparency on the activity and the transmission of information to customers while making the provision of the best service a priority in a highly competitive market;
- facilitate and support the insurance/investment process and communication between consumers and insurers/producers in a spirit of confidentiality and trust, empathy and efficiency;
- are an integral part of the (local) economic, social and territorial environment in which their clients operate;
- are important contributors to the economy in general and will play an increasingly important role in the transition to a sustainable economy in the coming years (risk management, prevention, awareness, innovation services and sustainable investment advice);
- act as information providers to consumers and as such help to increase financial literacy. They also "nudge" consumers to think about their risks, their pensions and their investments.

In a world with the economy in constant motion, insurance and financial intermediaries accompany the changes by providing solutions adapted to the new risks as close as possible to consumers and insurers.

From a competitive perspective

The insurance intermediation sector is characterised by the presence of many intermediaries. The majority of the 800,000 intermediaries in the EU are micro and SME scale undertakings with a local focus. They compete with one another. They only survive by being relevant in an extremely competitive environment where there is no compulsion to avail of their services.

Banks, internet operators and direct writers compete head-on with insurance intermediaries.

Companies in every sector of the economy work with intermediaries to find solutions for their risks in the national, European or international market.

Thanks to intermediaries more people and businesses are well insured.

Thanks to intermediaries, the European insurance market can export its capacity and know-how worldwide. Intermediaries make insurance more accessible to consumers and smaller businesses.

Reputation and trust are important factors that can only be built up over time. They can potentially be lost in an instant, and thus require ongoing attention and maintenance.

The added value of insurance intermediaries in the insurance sector

Introduction

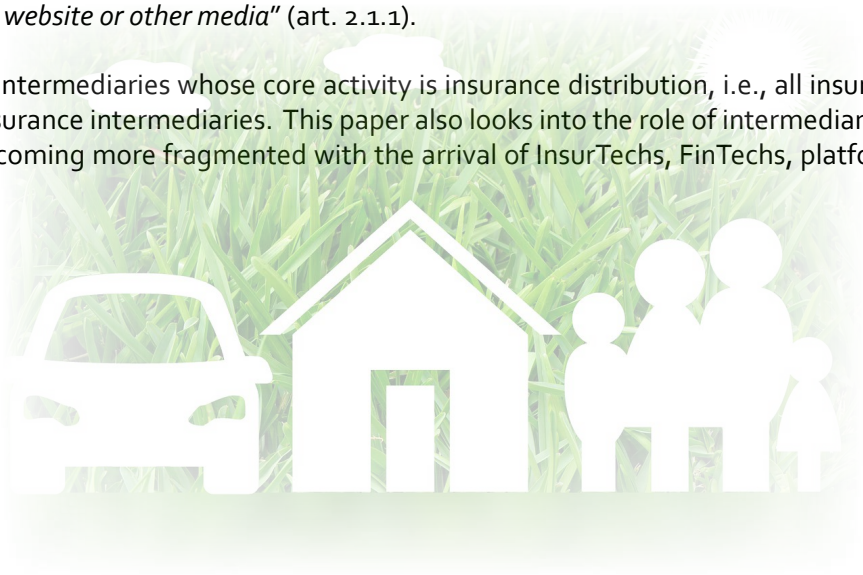
Insurance intermediaries play a key role in the insurance value chain.

The purpose of the present document is to highlight the contribution made by insurance intermediaries to the proper functioning of the European insurance market and the value they offer to insurance buyers and insurers.

The Insurance Distribution Directive (IDD) defines an insurance intermediary as "*any natural or legal person, other than insurance or re-insurance undertaking of their employee and other than an ancillary insurance intermediary, who for remuneration takes up or pursues the activity of insurance distribution*" (art.2.1.3)[1].

Moreover, according to the IDD, insurance distribution includes not only selling insurance contracts but also post-sale activities such as helping their customers and their insurers with the management of any claims arising from an insured event. More precisely, the IDD defines insurance distribution as "*the activities of advising on, proposing, or carrying out other work preparatory to the conclusion of contracts of insurance, of concluding such contracts, or of assisting in the administration and performance of such contracts, in particular in the event of a claim, including the provision of information concerning one or more insurance contracts in accordance with criteria selected by customers through a website or other media and the compilation of an insurance product ranking list, including price and product comparison, or a discount on the price of an insurance contract, when the customer is able to directly or indirectly conclude an insurance contract using a website or other media*" (art. 2.1.1).

This document focuses on insurance intermediaries whose core activity is insurance distribution, i.e., all insurance intermediaries other than ancillary insurance intermediaries. This paper also looks into the role of intermediaries in the insurance value chain which is becoming more fragmented with the arrival of InsurTechs, FinTechs, platforms, etc.



[1] An ancillary insurance intermediary is defined in the IDD (art. 2.1 (4)) as "any *natural or legal person, other than a credit institution or an investment firm as defined in points (1) and (2) of Article 4(1) of Regulation (EU) No 575/2013 of the European Parliament and of the Council (12), who, for remuneration, takes up or pursues the activity of insurance distribution on an ancillary basis, provided that all the following conditions are met: (a) the principal professional activity of that natural or legal person is other than insurance distribution; (b) the natural or legal person only distributes certain insurance products that are complementary to a good or service; (c) the insurance products concerned do not cover life assurance or liability risks, unless that cover complements the good or service which the intermediary provides as its principal professional activity."*

Regulation of the insurance intermediaries and their activities

The activities of insurance intermediaries are tightly regulated, and the transposed IDD is the main legal instrument concerning insurance intermediaries in the Members of the European Economic Area (EEA)[2].

The IDD is a minimum harmonisation Directive meaning that Member States cannot implement less than what is required by the IDD, but they may introduce additional measures to ensure the protection of their consumers.

The IDD provisions are further specified by regulations and two EU delegated regulations in particular cover:

1. product oversight and governance requirements for insurers and insurance distributors; and,
2. information requirements and conduct of business rules applicable to the distribution of insurance-based investment products (IBIPs).

The Commission also adopted an implementing technical standard (ITS) regarding a standardised format of the IDD Insurance Product Information Document (IPID), and a regulatory technical standard (RTS) reviewing the minimum amounts of PII/financial capacity. The IDD came into force on 23 February 2016 and had to be transposed into the national laws of the EU Member States by 1 July 2018. As of February 2020, all EU Member States had implemented the IDD.

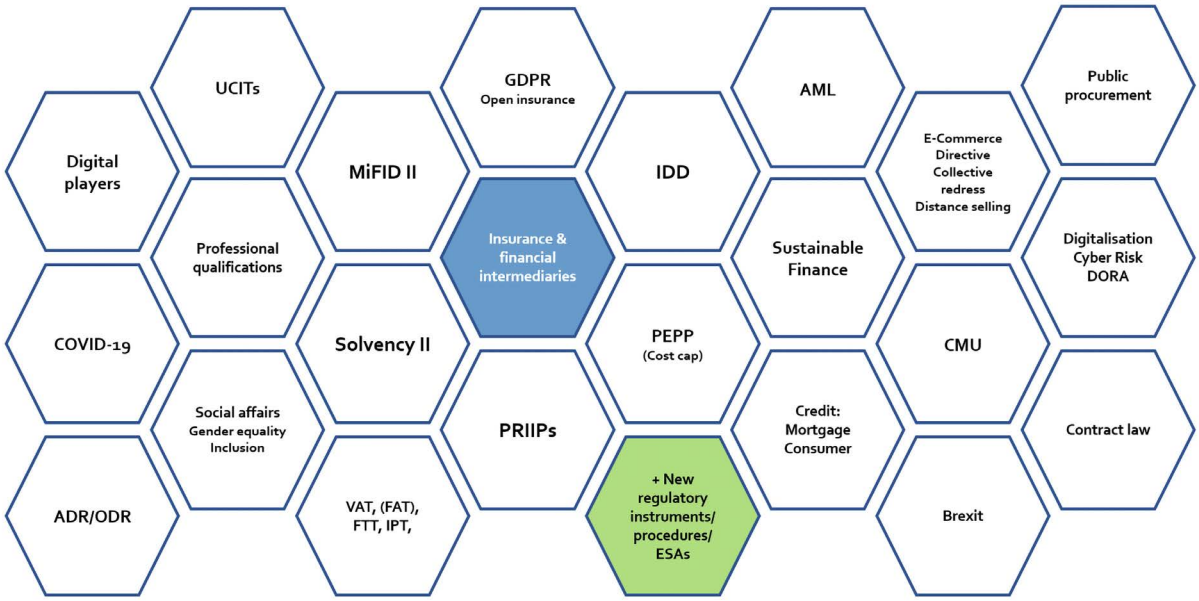
In addition to the key IDD requirements and obligations listed in Box 1, insurance intermediaries are also subject to a range of other EU directives and regulations (Figure 1).

Main IDD features for insurance intermediaries

- Requirement to be registered and supervised with relevant competent authority
- Have appropriate knowledge and ability, and Continuing Professional Development (CPD) to be undertaken regularly
- Be of good repute
- Have professional indemnity insurance
- Have measures to protect customers against inability to transfer the premium /amount of claim or return premium to the insured.
- Act honestly, fairly and professionally in accordance with the best interests of customers
- No remuneration that conflicts with the duty to act in the best interest of customers
- Disclosure of the nature and basis of the remuneration
- Specific requirements for sale of insurance-based investment products
- Product Oversight and Governance (POG) requirements

- Box 1 -

Figure 1 - Overview of EU rules applicable to insurance intermediaries



BIPAR Source

[2] The European Economic Area comprises the EU Member States, Iceland, Liechtenstein and Norway.

The general business model of European insurance intermediaries

The population of European insurance intermediaries (other than ancillary insurance intermediaries) is highly diverse, in terms of insurance intermediation activity they undertake, their size, the nature of their relationships with insurers and whether they are natural or legal person. Broadly speaking, in the EEA, the insurance intermediation sector comprises three major sub-sectors:

1. Global and multinational business insurance intermediaries, who serve major multinational and domestic firms, and provide a wide range of services to these clients in addition to the traditional brokerage services. They also serve a large part of the SME client market.

2. Major domestic intermediaries who provide services to larger and medium-sized companies. They also serve some of the national branches or subsidiaries of multinationals and small companies, and they are active in a variety of sectors and niches. Such intermediaries are likely to be present throughout the country in which they operate. Some intermediaries in this larger category also offer personal lines non-life insurance at large scale via, for example, affinity programs or offer services to other, smaller intermediaries.

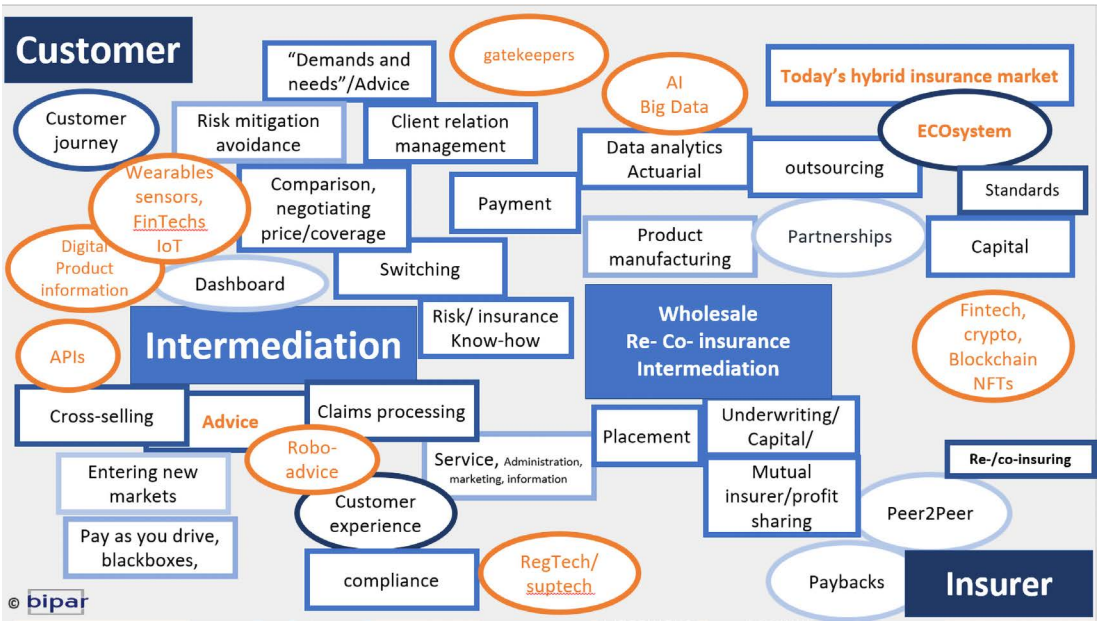
3. Smaller intermediaries who mainly serve the "small" end of the business spectrum and the personal lines market, and occasionally serve larger clients on a relationship basis.

Some of the intermediaries who fall into the latter two categories may belong to international networks. These arrangements allow smaller intermediaries to offer products to their clients in several countries.

Overall, most insurance intermediaries are small or micro-enterprises. They operate in small towns and villages where they serve local consumers.

However, irrespective of these differences in size, type of intermediation activity, etc., the general business model underlying the activities of an insurance intermediary is one in which the intermediary provides services to both the buyers of insurance products and the insurers or product manufacturers providing the insurance product(s) to the buyers (Figure 2).

Figure 2 - Today's hybrid insurance market is becoming the ecosystem



BIPAR Source

The range of services that an insurance intermediary may offer is wide and varies across intermediaries, in fact, some of the intermediaries' services shown in the generic business model are not offered in all Member States.

Insurance intermediaries intermediate in non-life (car, liability, household, ...) and life insurance including IBIPs or pensions or health and/or employee benefits services. Some intermediaries may intermediate in all these insurance products while others may focus specifically on non-life or life insurance. Moreover, within the non-life segment, some intermediaries may sell their services mainly to consumers and/or SMEs (such as car insurance, fire insurance, etc.) while others may specialise in insurance for larger commercial and industrial clients.

Insurance intermediaries may work exclusively with one or a few insurers or with a wide range of insurers. While the IDD does not provide for a distinct legal status for the insurance intermediary based on the nature of the legal relationship between the intermediary and the insurance undertaking, a number of Member States do and distinguish between insurance agents and insurance brokers (for example, Belgium, France, Germany, Italy, Romania, Spain):

- An insurance intermediary may be an agent of an insurance undertaking(s) and represent the insurance undertaking(s). The agent can commit the insurance undertaking(s) and performs the tasks that each of these insurers delegates or entrusts the agent with to provide service to clients. In the context of the digital evolution of insurance, the agent is also entrusted to "humanise" the remote relationship with customers by professionally and emotionally enhancing the digital interactions between the insurance client and the insurers.

- An insurance intermediary may interact with many insurers and/or not be the agent of these insurers. In a number of Member States, such an insurance intermediary is called an insurance broker. Typically, the insurance broker facilitates the insurance process between the insurance buyer and the insurance client. There is a variety of definitions in the various Member States.

- The client/intermediary relationship is typically a long-term relationship which mostly covers a series of insurance contracts.

- The IDD also specifies that, in the case of the sale of IBIPs "*Member States may require that, where an insurance intermediary informs the client that advice is given independently, the intermediary shall assess a sufficiently large number of insurance products available on the market which are sufficiently diversified with regard to their type and product providers to ensure that the client's objectives can be suitably met and shall not be limited to insurance products issued or provided by entities having close links with the intermediary*." (art. 29.3)

- Some intermediaries may not interact directly with insurers but do so through other insurance intermediaries.

- Irrespective of their precise legal status in the different Member States and the nature of their relationship(s) with insurers, all insurance intermediaries are required by the IDD to "***always act honestly, fairly and professionally in accordance with the best interests of their customers***" (art. 17.1).

All insurance intermediaries always have to ensure, prior to the conclusion of an insurance contract and on the basis of the information provided by the insurance buyer, that **the insurance product proposed to an insurance buyer meets the demands and needs of the customer** (art. 20.1)[3].

Moreover, the IDD requires insurance intermediaries to inform a client well before an insurance contract is signed whether or not they have a contractual obligation to exclusively distribute insurance products of one or several insurers. In both cases, the intermediaries are obliged to provide the customer with the names of the insurers with which they either have exclusive distribution arrangements or, if they do not have exclusive arrangements, the names of the insurers with which they may or do conduct business (art. 19.1)[4].

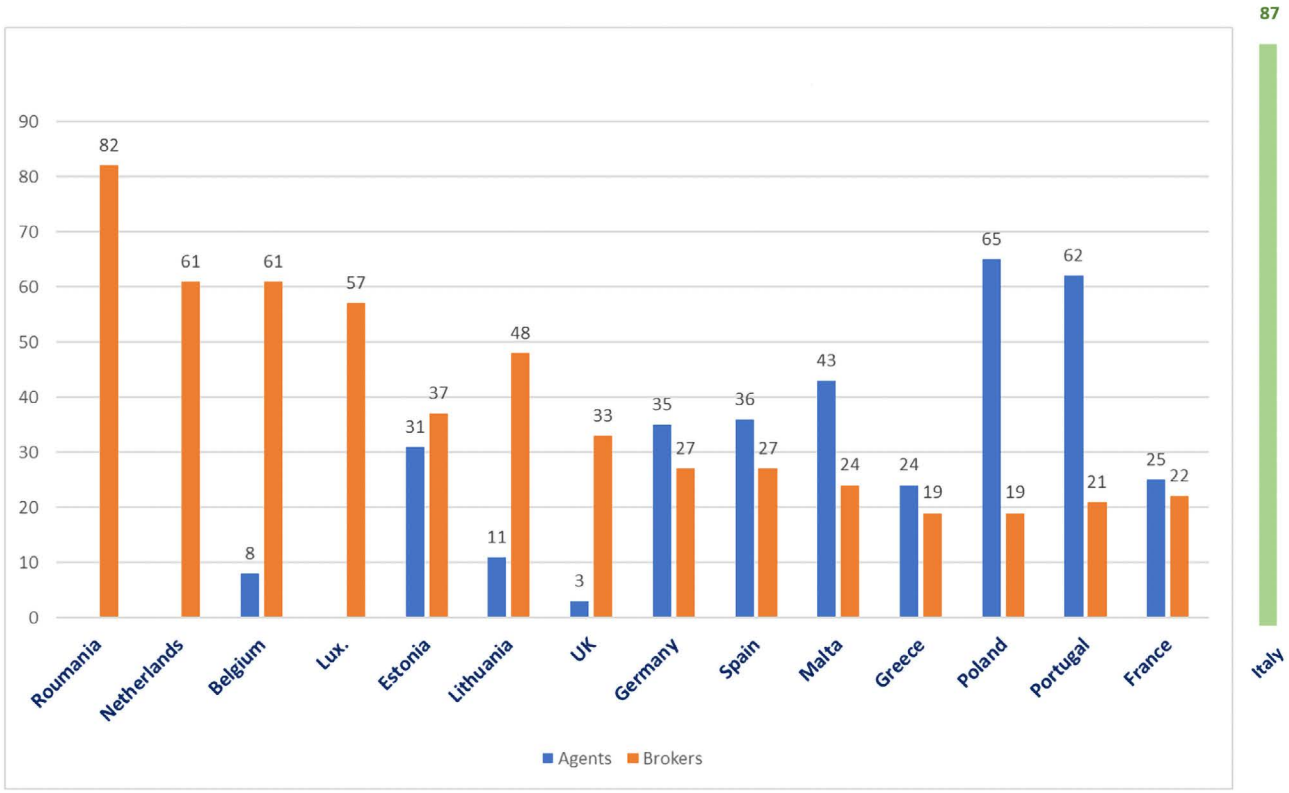
[3] Except in the case of the insurance of large risks
[4] Except in the case of large risks

The role of insurance intermediaries in the insurance value chain

Insurance products are distributed through three main channels to insurance buyers, namely 1) directly by insurers; 2) through insurance intermediaries other than credit institutions; and 3) through credit institutions acting as insurance intermediaries.

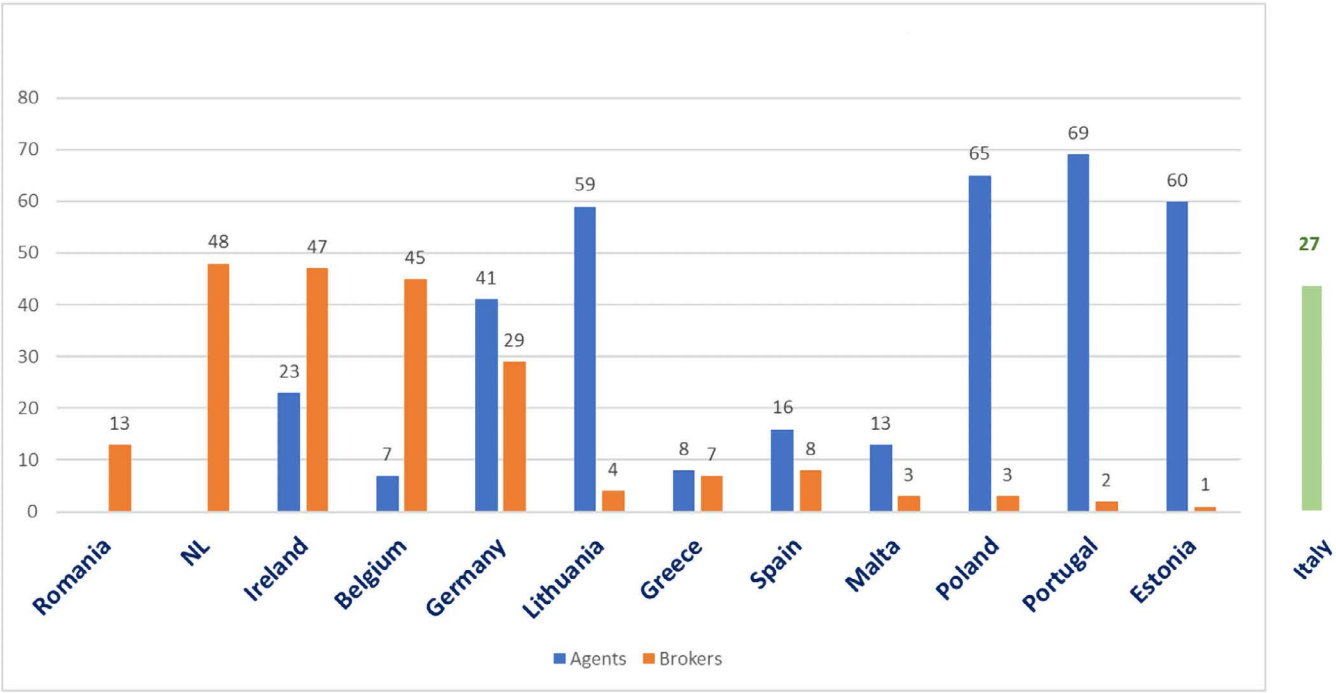
The EIOPA 2022 report shows that, in the EEA countries for which data exist on sales of insurance product by distribution channels, insurance intermediaries other than credit institutions play a major role in the distribution of both life and non-life insurance products in Europe. This is especially the case in the distribution of non-life insurance. Intermediaries accounted for the distribution of over 50% of gross written premiums (GWP)[5] for non-life insurance products in all Member States in 2020. Credit institutions acting as insurance intermediaries or bancassureurs account for a significant share of the distribution of life insurance products while they are less prevalent in the distribution of non-life insurance products.

Figure 3 - Non-life insurance market shares (2022 data)



[5] The gross written premiums are equal to the total premium (direct and assumed) written by an insurer before deductions for reinsurance and ceding commissions

Figure 4 - Life insurance market shares (2022 data)



Figures 3 and 4 are based upon information we received from our national associations.

The fact is that it is still as difficult as ever to find accurate data on insurance distribution in some countries. As a result, it is hard to compare markets as the classification and data collection methods vary from one market to another. Not all figures in both graphs can thus be considered as being "scientifically" correct, and this should be kept in mind when comparing the figures.

Both graphs only provide a general overview of the relative importance of respective distribution channels in the various markets.

For more details, please contact BIPAR or its national associations.

The **digitalisation** of the European economy manifests itself in the insurance sector through online insurance intermediation (directly via websites, mobile applications, e-mails, etc.). These digital channels are used by both insurance intermediaries and insurers. Very often the system is "hybrid" and combines human and digital interactions. While it is estimated that in Denmark and Estonia such online sales account for 80% of total GWP and in Lithuania for 70% for non-life GWP, in many Member States on-line sales still account for only a small proportion of total GWP (0.2% to 2%). However, this figure is projected to grow in the coming years.

In addition to a growing reliance on online or hybrid insurance intermediation, insurance intermediaries and insurers have also adopted various digital tools to increase efficiency in the different parts of the insurance value chain or Ecosystem (see section on the digitalisation of the insurance value chain.)

It should be noted that in addition to insurance intermediaries, there exists other categories of financial professionals who act as insurance distributors in combination with other activities, including:

- Financial investment advisors who provide recommendations on financial instruments or services with a focus on wealth management and often on retail investors;
- Wealth management advisors who provide advice on wealth strategy and organisation, which may include investment products, life insurance, provident funds, term accounts, savings accounts and savings books, credit broking as well as real estate or pension products;
- Credit or mortgage credit intermediaries who present or offer credit agreements to consumers, assist consumers by undertaking preparatory work or other pre-contractual administration for the set-up of credit agreements or even conclude credit agreements with consumers on behalf of the creditor.

Insurance intermediaries play not only a key role in the distribution of insurance products, but depending on their business model, they can also be important economic actors in the other parts of the insurance value chain shown in Figure 5.

Indeed, in addition to intermediation insurance between insurers and their customers, intermediaries may offer their clients and insurers one or several more services shown in Figure 2. The precise range of services offered by an insurance intermediary to insurance buyers and insurers depends on the intermediary's business model and varies across insurance intermediaries and Member States.

Figure 5 - Key activities of the insurance value chain

Source: based on EIOPA 2020 Discussion paper on the (re)insurance value chain and new business models arising from digitalisation

The various activities of insurance intermediaries

The various activities of insurance intermediaries are described below, starting with the core activity of sales and distribution.

Sales and distribution

Services provided by insurance intermediaries to insurance buyers

1. Information and advice

- **Search costs**

The market for insurance products is characterised by a wide range of suppliers and differentiated products on one side and customers with varying needs on the other. As a result, the market also exhibits imperfect information for both the customer and insurer, significant consumer search costs in order to find the best product and asymmetric bargaining power[6].

- **Emotions created decision-making biases**

Moreover, due to various cognitive biases and limitations, insurance buyers may find it difficult and complex to select the insurance product which best meets their needs. "*The complexities arise from issues such as evaluating the likelihood and magnitude of risks, assessing financial needs and choosing an insurance package. The difficulties arise because insurance buyers face difficulties to predict the likelihood and magnitude of highly unlikely and largely unfamiliar future events.*

The buyers also face difficulties in understanding risks. They fail in properly evaluating the extent, frequency and probabilities of risks, and in interpreting them correctly. They also face difficulties in choosing and evaluating insurance price, quality, and benefits, and in comparing different insurance products provided in the market"[7] and purchase decisions may be influenced by "*emotions such as affection, love, fear and anxiety. The emotions created decision-making biases. The biases can be the result of cognitive limitations, information processing and perception, problem organizing and cognitive styles*"[8].

- **Risk of focus on price only**

Due to these complexities and cognitive biases, insurance buyers may focus only on price and not pay much attention to the terms and conditions of the contract. Moreover, once they have bought insurance, policyholders may not always search the market at policy renewal time to avoid the "hassle" of searching again.

- **Importance of demands and needs test**

As part of the assessment of the demands and needs of a client, insurance intermediaries will identify the risks customers face and ensure that they make informed decisions about the risks they wish to insure. Intermediaries put their knowledge and expertise at the service of customers, who often only have imperfect knowledge and risk making ill-informed decisions with highly detrimental impact to their welfare. Intermediaries can also make it easier for customers to switch from one insurer to another and contribute to healthy competition in the insurance market.

- **Increased consumer welfare**

Insurance intermediaries also reduce search costs for customers who typically only purchase insurance products infrequently and are less aware of market offerings. Customers can significantly reduce time and efforts, i.e. the costs of searching for the "best" deal by using an intermediary to meet their insurance needs. Intermediaries help reduce the effective price of insurance by reducing search costs and improve consumer welfare by reducing customer detriment (e.g. through reduced mental toll). Not only do insurance intermediaries reduce search costs for their customers, but they also help customers overcome choice overload issues.

[6] London Economics (2014). Insurance intermediaries' remuneration.
[7] Rabihah Md.Sum and Norhafiza Nordin (2018), Decision-Making Biases in Insurance Purchasing, Journal of Advanced Research in Social and Behavioural Sciences, 10, Issue 2 (2018), pp. 165-179.
[8] Rabihah Md.Sum and Norhafiza Nordin (2018).

- **Importance of reputation**

As mentioned previously, insurance buyers often lack the knowledge and expertise required to identify the "best" insurance product and provider for his/her needs. Intermediaries would suffer severe damage to their reputation if it were known in the marketplace that they recommended placing insurance with an insurance provider that has the reputation of being unreliable in paying claims correctly[9].

- **Aligned interests**

Because of the potential damage to reputation, the incentives of the intermediary are aligned with those of their clients as well as those of the insurance provider. In short, because of its repeated interactions with insurance companies and clients, the intermediary helps overcome the imperfect information that would otherwise hamper the market.

- **Recommendations and advice**

Once the risks of the client are identified and the insurance needs are defined, there are a number of factors determining the recommendation that intermediaries make to their clients when advising them on the choice of a particular insurance or insurer.

Apart from the price, these factors include, inter alia:
- the breadth of coverage available (capacity);
- the insurer's flexibility in agreeing coverage;
- the insurer's image and reputation, especially in respect of claims service (speed, fairness of settlements, additional benefits to claimants);
- the quality and clarity of documentation provided;
- the insurer's speed in issuing documentation or in quoting terms;
- timeliness in inviting renewal;
- the technical competence of the insurer's staff;
- the quality and availability of advice provided to policyholders;
- the quality of the other services provided by the insurer, his locational proximity.

This list of additional factors highlights clearly that price is not the only determining factor in the choice of insurance.

- **Comparison websites**

The development of online comparator platforms has reduced search costs for mass-market insurance products such as car insurance, but it is not clear how these platforms meet the IDD "demands and needs" test in their recommendations to prospective insurance buyers.

Due to the various potential decision biases presented earlier, the reliance on platform information may lead to an over-emphasis of price in the product choice decision of the insurance purchaser

Under the IDD, insurance intermediaries may only provide information or may also provide advice. However, as already noted, irrespective of whether advice is provided or not, insurance intermediaries have to ensure that any insurance product they propose to a customer meets the customer's demands and needs.

Moreover, by being able to engage in a discussion with a customer seeking to purchase a particular insurance product, insurance intermediaries are well placed to provide advice if the client so wishes.

- **Advice**

To avoid any confusion about the nature of the services offered by an insurance intermediary, the latter has to inform the client well prior to the conclusion of insurance contracts whether or not the intermediary provides advice, and if advice is provided, whether such advice is based on a fair and personal analysis (art. 19.1)[10].

Irrespective of whether advice is given, prior to the conclusion of any insurance contract, insurance intermediaries always have to give their customers "*objective information about the insurance product in a comprehensible form to allow the customer to make an informed decision*" (art. 20.1).

In addition, when advice is provided, insurance intermediaries have to give their clients "*a personalised recommendation explaining why a particular product would best meet the customer's demands and needs*" (art. 20.1), and when the advice is given on a fair and personal basis, it needs to be based on a "*sufficiently large number of insurance contracts available on the market*" (art. 20.3).

[9] This is a situation in which people have a difficult time making a decision when faced with a wide range of choice and many options.
[10] This obligation does not apply in the case of large risks.

- **IBIPs**

When the insurance product sold by the insurance intermediary is an IBIP and the client receives advice from the intermediary when purchasing the product, the latter will have to inform the customer whether he/she will provide a periodic assessment of the suitability of the product recommended to the customer (art. 29.1(a)). In addition, the insurance intermediary will have to provide information and warnings of "*the risks associated with the insurance-based investment products or in respect of particular investment strategies proposed*" (art. 29.1(b)) and "*information relating to the distribution of the insurance-based investment product, including the cost of advice, where relevant, the cost of the insurance-based investment product recommended or marketed to the customer and how the customer may pay for it, also encompassing any third party payments*" (art. 29.1(c)).

2. Reduction in asymmetric bargaining power

Smaller and medium-sized insurance buyers may be subject to the bargaining power of large insurance providers when dealing directly with such providers (London Economics, 2014).

As intermediaries place a considerable amount of business with insurance providers, they are in a position to obtain better terms for their smaller and medium-sized clients than the latter would be able to obtain directly. For example, a number of intermediaries have developed schemes to aggregate risks.

Additionally, many intermediaries develop specialist schemes and facilities based on their in-depth knowledge of a particular sector. This knowledge and the ability to aggregate risks enable them to negotiate better terms and broader policy conditions for their clients. Such schemes are usually accessible to other intermediaries

Services provided by insurance intermediaries to insurers

Insurance intermediaries reduce the distribution costs for insurers and facilitate entry into the market of new insurance companies, by providing them with access to a large client base, without having to incur the high fixed costs of building a distribution network. By helping reduce barriers to entry and expansion, intermediaries support healthy competition in the insurance market.

Insurance intermediaries also help promote and advertise insurers' products and services.

Insurers also use intermediaries also because of their efficiency and level of service.

Finally, insurance intermediaries reduce the uncertainty facing insurance providers. Insurance buyers have an incentive to represent the risk as being a low probability risk so as to pay an as-low-as-possible premium.

Moreover, once insurance has been obtained, the insurer faces the classical moral hazard issue – that the insured party may not necessarily take all the appropriate measures to prevent the risk from materialising. As intermediaries depend on repeat transactions with insurance providers and their reputation for their livelihood, they have every incentive to solicit and present risk information in a balanced and professional manner to insurance providers.

The intermediary also informs the client about his/her own ongoing responsibilities in the framework of the insurance contract, thereby helping reduce moral hazard.

Post-sale service and assistance

Services provided by insurance intermediaries to insurance buyers

Insurance intermediaries will help their clients with any contractual issues and address queries that policyholders may have during the life of the insurance contract. For example, a policyholder may have a question several months after the conclusion of an insurance contract about whether, as part of a policy, cover is provided for a particular event or whether the cover would need to be changed due to changes in personal circumstances.

Services provided by insurance intermediaries to insurers

Intermediaries can provide for insurers all or part of the typical customer relationship management services.

Claims management

Services provided by insurance intermediaries to insurance buyers and to insurers

Insurance intermediaries assist their clients and insurers with administrative procedures, e.g. with claims related, contract and policy administration services.

Product design and development

Services provided by insurance intermediaries to insurance buyers

To meet the needs of some of their clients, insurance intermdiaries may design new and innovative solutions to cover not frequently insured risk or to offer life cycle-related or assets-related protection solutions

Services provided by insurance intermediaries to insurers

Based on the needs and demands of their clients, insurance intermediaries may suggest new potential products to insurers or may actually work together in developing a new insurance product which the insurance intermediary may than distribute to other insurance intermediaries.

Pricing and underwriting

Services provided by insurance intermediaries to insurers

Insurance intermediaries may provide risk analysis and advice to underwriters.

The contribution of insurance intermediaries to the digitalisation of the European economy

Digitalisation is resulting in many transformations of the insurance value chain[11] and insurance intermediaries have risen to the challenge. They contribute to the digitalisation of the European economy by making increasing use of online channels for selling their services to insurance buyers and by adopting various digital tools for many of their activities and services.

Most intermediaries have adopted new ways to remotely operate and sell insurance products such as new payment and communication methods in the form of mobile apps or chat boxes, or claim handling methods in the form of online consultations and other online tools, such as video-appraisals and digital signatures (EIOPA[12]). Digitalisation also makes it easier for the intermediary to follow the entire life cycle of the insurance service provided to a client, from distribution to after-sales service.

Most intermediaries and customers value a "hybrid" approach that combines the flexibility and efficiency of digital tools with the physical presence and human interaction (Accenture[13]). This allows intermediaries to serve customers at different ends of the spectrum in terms of digital inclusion and capabilities with access to insurance. Maintaining the physical presence and human approach allows intermediaries to provide personalised and "emotional" assistance in times of claims and crisis.

Artificial intelligence is also increasingly in use in some parts of the insurance value chain. There are increasing calls in the industry to introduce regulation addressing ethical, quality of service and data privacy concerns related to the use of these emerging technologies in the sector (EIOPA, 2022).

[11] See, for example, Antonella Cappiello (2020), The Digital (R)evolution of Insurance Business Models, American Journal of Economics and Business Administration, Vol. 1, pp 1- 13 and EIOPA (2020), Discussion Paper on the (Re)insurance value chain and new business models arising from digitalisation.
[12] EIOPA. (2021). Consumer Trends Report 2020.
[13] Accenture. (2021). Redéfinir pour croître.

Intermediaries play an important role in the Capital Markets Union

Insurance intermediaries help mobilise European citizens' savings for financing the digital and environmental transition

As already noted above, insurance intermediaries (and some other financial intermediaries) sell IBIPs. The range of types of IBIPs is wide (see Box 2) and, depending on a person's circumstances can be very useful longer-term savings instruments. However, such instruments are typically complex and, like any other investments, involve some risks. These characteristics together with the fact that, due to various cognitive and behavioural biases, many individuals do not focus on proper financial planning, especially for their retirement and may result in under-investment for retirement. The biases identified in a recent EIOPA paper include "cognitive and behavioural biases such as focus on the present (preference of consuming today over saving), inertia (people know they should save for old age but are reluctant to engage with a future and complex subject), projection bias (people overestimate the degree to which their future preferences remain the same as in the present), or reference dependence (people make decisions involving loss and risk in relation to a particular reference point)[14].

Moreover, people also tend be overwhelmed when faced with too much choice ('choice overload') and may decide not to invest at all and keep their savings in saving deposits or similar financial instruments which are simpler to understand and perceived to be "safer".

Intermediaries also observed that, when they discuss finances with clients/ consumers, people do not always have the factual information at hand. In particular, people have little information on statutory pensions and some people do not have a good picture of their long-term demands and needs.

Typical insurance-based investment products

- Unit-linked or index-linked life insurance
- Whole of life insurance with profit participation used to reduce the maturity
- Endowment insurance with profit participation (regular premiums or single premium)
- Deferred annuity insurance with profit participation;
- Capital redemption products with participation features;
- Traditional capital life insurance cover; and
- Hybrid products

- Box 2 -

Source: EIOPA (2022) Annexes to EIOPA'S Consultation Paper on retail investor protection

To address this basic information gap, insurance intermediaries can help people collect and compile the required information before even entering into a conversation about demands and needs, choices, appropriateness, or suitability tests.

The person-to-person interaction with the intermediary, the presentation and explanation of the information given to the prospective IBIP buyer, and any advice given, help reassure buyers and overcome their initial cognitive and behavioural biases.

Through their various activities, insurance intermediaries contribute in mobilising the pool of savings for investments for a stronger, greener, digital, inclusive and resilient European economy by making financing more accessible to European companies.

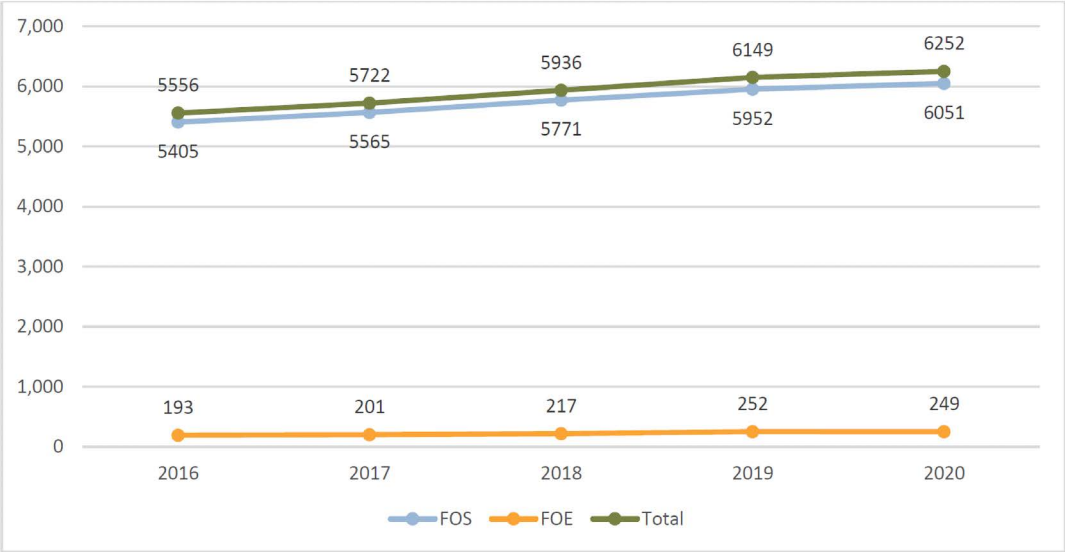
Furthermore, many consumers need to be "nudged" to think and talk about their finances or future financial needs.

[14] EIOPA (2022) Annexes to EIOPA's Consultation Paper on retail investor protection.

Insurance intermediaries contribute to the development of the Single Market in financial services

There has been a steady increase in the number of insurance intermediaries operating with a passport for the freedom to provide services (FOS) or freedom of establishment (FOE) in the EU between 2016 and 2020 (EIOPA, 2022a) (Figure 6). While passports allow intermediaries to conduct cross-border business, it is important to note that the number of passports or cross-border notifications[15] does not provide information on the actual extent to which insurance intermediaries make use of their passports and actually engage in cross-border compared to domestic business.

Figure 6 - Number of insurance intermediaries with a passport (2016-2020)



Source: EIOPA (2022) Report on the application of the IDD

An earlier study[16] by EIOPA also examined the share of domestic intermediaries with a passport and cross-border business in terms of share of total GWP, as reported by insurers. That 2018 study focused on data for the period of 2013 to 2017 and found only limited correlation between the two variables.

Cross-border insurance intermediary business (as a percentage of total GWP) was particularly high in smaller countries such Estonia, Ireland and Luxembourg (above 50%) and Belgium, Liechtenstein, Lithuania and Malta (between 30% and 50%) but remained more limited in most countries. The EEA average of cross-border business as a percentage of total GWP stood at around 10%.

Moreover, the study found that a significant share of intermediaries' cross-border notifications relates to neighbouring Member States, e.g., 36% of the total number of intermediaries' notifications received by the Portuguese National Competent Authority were to conduct business in Spain.

Finally, as already noted earlier, the existence of intermediaries means that it is not necessary for new insurers to build up a distribution system in order to enter new insurance markets. This can be especially challenging and costly for cross-border entry by insurers.

In particular, under the commission system, there is no fixed cost for the insurer or the client. The commission system ensures a mutualisation of costs and easy access to an intermediation service as the commission system is a "no cure no pay system".

Intermediaries provide a distribution channel for new entrants and, as a result, insurers do not have to incur the large, fixed costs associated with rolling out a distribution system; they only have to carry the costs associated with dealing with the risks which intermediaries present to them. For example, a number of international insurers have entered the EU business insurance market over the last 10 to 15 years. Without insurance intermediaries, these new carriers would have found entry into the market very, if not prohibitively, costly because they would have had to build up a distribution network de novo.

[15] i.e. insurance intermediaries notifying of their intention to provide services cross-border without having to report actual business
[16] EIOPA (2018) IDD – Evaluation of the Structure of Insurance Intermediaries Markets in Europe

Insurance intermediaries, comitted players in the climate transition

Close to their customers, the intermediaries who are members of BIPAR's national associations, are one of the "cornerstones" for promoting the distribution of "sustainable" financial and insurance products throughout Europe. Raising awareness of the climate change issue will be a long-term task for which the intermediaries represented by BIPAR and its member associations, will be indispensable.

As actors in the fight against global warming, they create risk awareness and are able to offer products and services to protect oneself against the consequences of climate change, whether it be the risk of flooding, severe drought or rising water levels.

Intermediaries are the first to notice the losses (and human suffering) linked to the progression of extreme meteorological events, and they know how to propose solutions as close to the ground as possible, whether in rural or urban areas, and thus strengthen insurance coverage or help clients and insurers to manage certain risks in an innovative way that has become sometimes difficult to insure. Indeed, according to a report quoted by the European Commission, "a 1% increase in insurance coverage could reduce the cost of climate-related disasters borne by taxpayers or governments worldwide by 22%".

How are intermediaries remunerated for their services?

Under the IDD, insurance intermediaries can be remunerated for their services through:

- a fee paid by the customer; or,
- a commission that is included in the insurance premium; or,
- an economic benefit of any kind offered or given in connection with the insurance contract; or,
- a combination of these forms of payments (IDD art. 19.1(e)).

In the case of sales of IBIPs, insurance intermediaries may receive fees or commissions from insurers provided such payment or benefit "*does not have a detrimental impact on the quality of the relevant service to the client*" and "*does not impair compliance with the insurance intermediary's or insurance undertaking's duty to act honestly, fairly and professionally in accordance with the best interests of its customers*" (IDD art. 29.2).

Member States may limit or prohibit the acceptance of fees, commissions or other monetary or non-monetary benefits paid or provided to insurance intermediaries in relation to the distribution of insurance products (IDD art. 22.3 for non-IBIP products and art 29.3 for IBIPs).

In all cases, in good time before the conclusion of an insurance contract, the insurance intermediary's customer is to be informed of the nature of remuneration received in relation to the insurance contract.

The remuneration of the intermediary through a commission has been a major contributing factor to the successful and competitive development of insurance markets all over the world. In the choice between commissions or fees, it is not only the size of the business that is important. Equally important are the nature and/or level of sophistication of the services required and the specific levels of service which are agreed. In any case, the decision to work on a fee or commission basis is a decision that should be taken between the parties based upon a transparent dialogue on the various options.

In a number of insurance lines and countries, insurance intermediaries offer the choice to the client to work either on a commission or a fee basis. When considering the choice between the two, the following factors are generally considered by both the intermediary and the client in their dialogue.

Commission is only payable if a contract ensues. A fee system creates uncertainty about the future cost, both at the time when the insurance is being effected, and when a claim occurs or when other services are rendered by the intermediary. In a fee system, clients should consider if they will be able to afford to pay fees based on time spent in the event of a claim.

The commission system satisfies a need for services in the future. The consumer purchases a "product" that, at the time of acquisition, is incomplete. In addition to the guarantee, it comprises a whole range of services (issuing of policies, collecting of premiums, treatment of claims, amending the policy and sometimes advancing compensation) which are not quantifiable at the time of the purchase.

The commission system offers a form of service contract against the cost of the provision of services by the intermediary following the purchase of the insurance product whereby the intermediary will give service at no extra charge in the event of any service being required other than at the inception or renewal.

From an economic perspective, overall, there exists no system which is preferable in all circumstances and the coexistence of various remuneration systems, and, in particular, the freedom to decide on the remuneration systems between the parties is the best guarantee for competitive, efficient and dynamic markets that work for the client and that avoids advice gaps.

The 2022 report by EIOPA found that the commission-based model remains the prevailing practice in most Member States (Austria, Belgium, Bulgaria, Czechia, Estonia, Finland, France, Germany, Ireland, Italy, Latvia, Lithuania, Malta, Poland, Portugal, Romania, Slovakia, Slovenia, Spain and Sweden).

Moreover, the study noted that:

- 6 Member States (Croatia, Denmark, Finland, Netherlands, Romania and Slovakia have limited or prohibited the acceptance or receipt of fees, commissions or other monetary or non-monetary benefits in relation to the distribution of any insurance product (Article 22(3) of the IDD); and
- 9 Member States (Croatia, Czechia, Finland, Ireland, Italy, Netherlands, Romania, Sweden and Slovakia) have prohibited or further restricted the offer or acceptance of fees, commissions or non-monetary benefits from third parties in relation to the provision of insurance advice on IBIPs (Article 29(3) of the IDD).

Conclusion

Insurance intermediaries play a key role in the insurance value chain.

There are many types of intermediaries and insurance distributors who are in competition with one another.

Insurance intermediaries highly contribute to the well-functioning of the European insurance market and they offer services and value to the insurance process, to insurance buyers and to insurers.

The IDD is a modern activity-based Directive that contributes primarily to the protection of the consumer.

Insurance intermediaries help mobilise European citizens' savings for financing the digital and environmental transition.

bipar

The European Federation of Insurance Intermediaries

BIPAR
Avenue Albert-Elisabeth 40 - 1200 Brussels - Belgium
Tel : +32-2-735.60.48 - bipar@bipar.eu - www.bipar.eu