Broker Headaches

Business challenges for today's broker | 25 October 2007

What happens when the FSA comes knocking

The FSA's Arrow teams are about to swoop: is your business ready? Anita Anandarajah reports

Visits from the FSA – known as Arrow visits – have got brokers worried. Those that have already been visited refuse to speak out, citing "commercial confidentiality", and those that haven't, don't know what to expect.

So here's the truth about Arrow visits. The FSA designed the programme to help it measure the risks a firm poses to market confidence and consumer protection, thus fulfilling its statutory remit to reduce financial crime and promoting public confidence in the financial system.

The Arrow programme has two strands – the Arrow Firms approach and the Arrow Themes approach.The former involves assessing risks within a firm; the latter involves studying risks across several firms.

Not every broker will be subject to an Arrow visit. An FSA official, who was involved in designing Arrow II over the past three years, says the Arrow assessment is carried out on only five to six per cent of the 29,400 firms that come under FSA regulation. Of these, brokers represent an even smaller proportion.

"The remaining 95% are small firms that encounter sample-based assessment, known as thematic visits," he explains.

Advanced planning

There are 40 or so broking firms large enough to undergo an Arrow Firms assessment. These visits are planned in advance, usually with a month's notice.

The firms already know which they are as each will have been allotted a relationship manager who is a full-time FSA employee.

It is the FSA's policy not to name these companies, but it is known that large brokers like Aon, Marsh and Willis have had visits.

According to FSA estimates, some 40 to 45 general insurance retailers have undergone Arrow visits since March 2006, with another 15 to receive such visits in the next year.

These are the lucky ones that will experience Arrow II – a revised and improved form that was introduced last year, following concerns surrounding poor communication between the FSA and the inspected firm, and a lack of supervisory skills.

Natasha Peacock, legal consultant at Beachcroft, which provides consultation to

firms preparing to undergo Arrow visits, says: "Arrow II has brought about mostly positive changes."

To help employees of a firm understand the purpose of the visit, FSA staff now conduct a presentation on what the Arrow visit is about before they launch into the interview.

FSA staff have also been trained in how to conduct visits. They attended a two-week residential course last year, which Peacock says will put to rest worries that the FSA won't understand the business or the sector and, therefore, will not obtain a good picture of the firm's operations.

Peacock adds that FSA inspectors are now more "gentle" - meaning that the visit is more like a fact finding interview than an interrogation.

Guidance failure

A survey conducted by Beachcroft in 2005 found that more than two-thirds of firms (69%) were frustrated by the FSA's failure to provide guidance on how they could lower their risk assessment rating under the original Arrow programme. So the FSA now conducts a feedback session to make the firm aware of the FSA's findings before a letter is sent after the visit.

The letter should give a broad overview of what risks the FSA has identified within the firm and what the regulator would like the firm to do about it.

The letter will also mention the score for the level of risk and highlight specific areas for improvement.

Revisions to the inspection programme should mean that, for the properly prepared firm, an Arrow visit is not too much of a headache.

But, as Peacock observes, brokers tend to be nervous because the visits set the tone for their relationship with the financial services watchdog.

"The belief is that if you have had a good visit, then the FSA is likely to have a lighter touch with you. Conversely, a bad visit will mean closer scrutiny from the FSA, which will mean the costs of making your communication clearer will rise," she explains.

So, for nervous brokers, *Insurance Times* has compiled 12 top tips on how to handle an FSA interview. ➔

What to do when

Twelve top tips on how to dodge the FSA's arrows

1 It is important that the FSA staff have a pleasant space to work in. Don't put them in a broom cupboard, especially if they are around for a week.

2 Be proactive. If there is anything you think the inspectors should see to give a better perspective of the company, for example, an employment handbook, suggest that you'd like them to see it.

3 Appoint a member of your staff to be responsible for the visit, so that the FSA team has only one person to deal with. This is normally the head of compliance or the head of human resources.

4 Take notes of exchanges between your firm and the FSA team, but first ask permission. Don't read anything into it if they refuse. This could be the case if there is to be a one-to-one meeting with a non-executive director. Note-taking is important because if, say, you promise to send a report to the FSA within six months, you will be reminded of this when you look at the notes.

5 Treat this like a mini-project. Decide what you want to gain from the visit. Give the FSA the impression that you have a well-run business with good governance. Reduce the risk of having a lot of actions on your Risk Mitigation Programme. For example, if a broker doesn't have a client money system, the FSA will want a complete retrospective review which can be time-consuming and expensive.

6 Ensure your staff are comfortable talking about hot topics, like the selling of payment protection insurance, which is a topical issue for the FSA. And if a key manager has resigned, make sure that everyone is 'on message' so that the FSA team is clear about the circumstances.

7 It is recommended that companies rehearse an FSA interview. Prepare responses to questions you don't want to be asked. Make sure other people are aware of your concerns about any particular issues.

an inspector calls

12 The FSA will produce a draft letter and a draft of the Risk Mitigation Programme, which will provide an outline of the issues it has identified in your company. In reply, the company can comment only on factual inaccuracies, not on the judgments.

11 When planning the interview schedule, allow a 30-minute break for refreshments. This is not only for the FSA officers to rest, but so the person managing the visit can ensure they are satisfied with the arrangements and availability of documentation. You will need to keep track of documents you have provided.

10 Make sure relevant staff are properly briefed, so as to have a consistent message on the company's business activities. For example, a small broker may not have a dedicated risk management department, but the FSA would expect the firm to be able to assess the risks it runs and know its future plans.

9 It is important that at the end of each session, the person running the visit goes to the FSA team to ensure they have everything they need. At the end of the visit, the FSA team will sometimes hold a meeting to give an indication of issues to be raised in the Risk Mitigation Programme.

8 If you have a nervous staff member who is likely to be interviewed, suggest steps to make him feel more comfortable, such as have him prepare a mini-presentation. This could give him more confidence when he discusses his work with the FSA representatives.

Arrow themes

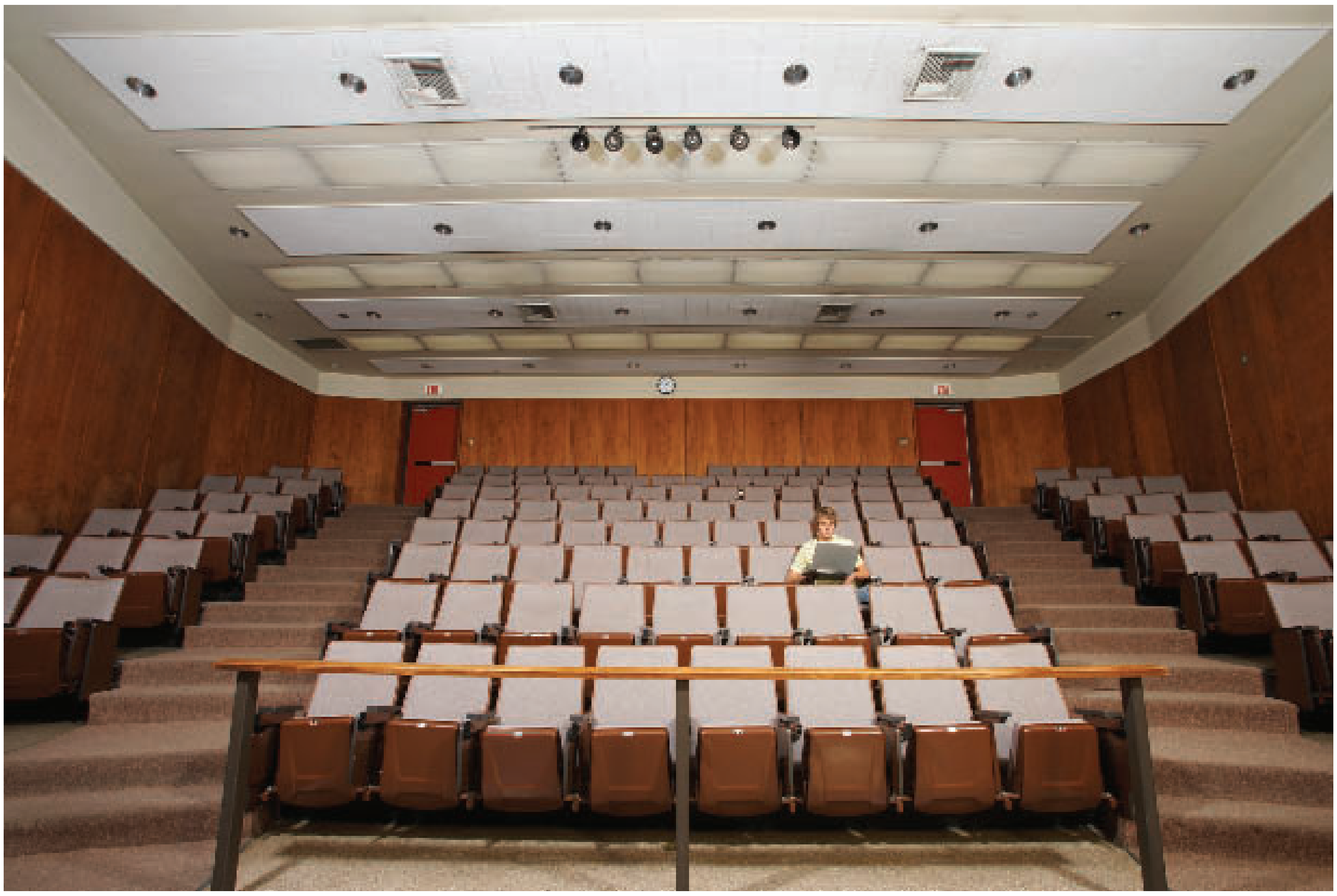
Handy hint: the FSA issues an annual business plan in February where it sets down its priorities for the year. This is a good place to look out for some of the hot topics that could emerge during Arrow visits. For the year 2007/08, these include:

- The sale of payment protection insurance and subsequent follow-up work, including enforcement investigations with individual firms
- The review of the handling of client money within general insurance brokers
- Current market practice on the identification and management of conflicts of interest
- Treating customers fairly
- Financial capability, which looks at what firms can do to think about the clarity of product literature so that customers understand what they've been sold
- Transparency of pricing and commission disclosure.

Read the FSA's *Risk Assessment Framework 2006* for what the FSA looks out for at: http://www.fsa.gov.uk/pubs/policy/bnr_firm-framework.pdf

Anyone for insurance?

Investment banking is proving a big draw for graduates seeking a financial services career, even though insurance has just as much to offer. Anita Anandarajah discovers why



The insurance industry deals with worldwide catastrophes on a daily basis, but as businesses, there is a far more prosaic challenge to face: recruiting and retaining top quality staff.

Lloyd's chief executive Richard Ward recently acknowledged the scale of the problem, declaring that the market faces a huge shortfall in recruiting claims professionals and financial modelling experts.

The figures tell their own story: 11% of graduates want a career in investment banking, but only 2.5% choose insurance, according to online job service Milkround.com.

In the face of such apathy, how can brokers large and small attract, and retain, the best talent?

The answer, it seems, may lie in self-promotion and training.

Former Biba chief executive Mike Williams confesses that the industry hasn't done enough to inform people of the career options available in the UK and globally.

"Investment banks have spent many years building relationships with universities and colleges. They are in an enviable position whereby a good student looking for a diverse, well-paying career would look at them first," he says. "They have contacts, literature and people within the institution that promote that proposition."

It would seem that brokers should be looking to hire more graduates. But, surprisingly, many still believe that school leavers are a safer bet.

Williams says: "You have someone who has shown a certain amount of academic aptitude, is still willing to learn and has not been moulded into certain attitudes by high level education."

Yet he acknowledges that insurance would benefit from sharing the attitudes of its City competitors: "Clearly we need graduates and high calibre candidates. There is evidence of this demand – the big brokers and insurers look enviously at how accounting firms continue to prosper by recruiting these people.

"Major brokers are tackling this issue more seriously than in the past."

Academic qualifications

Perhaps the answer lies in the all-embracing approach taken by broking juggernaut Towergate. It recently abandoned its graduate scheme in favour of a talent recruitment programme which "encompasses all walks of life and academic qualifications".

Fiona Andrews, Towergate's head of people development and reward, says: "A fairly staid scheme would limit the people we take in.

"We want innovative and clever people. They could be A-level holders, graduates, people who have changed roles and graduates who are moving from another industry."

Andrews admits that, whatever their background, it can be a struggle to attract people to choose insurance as their first career choice.

"We get a lot of financial graduates, but broking recruits tend to come from other broking industries as they tend to move around the market over the years."

Global brokers have a better hand to play with. Lynne Stannard, director of human resources at Aon, says: "We know what people are looking for – sponsorship to achieve professional qualifications, the opportunity to travel, the flexibility of working hours, a good career path and the opportunity to progress quickly through the ranks."

If insurers are ever to rank with glamorous investment banks when ➔

It's about looks, and money

A look at the career preference figures of an online job search service for graduates gives a good indication of the unpopularity of insurance.

On the Milkround.com database of more than 320,000 students and graduates, 40,333 have specified business and management in their career preferences, 35,043 for banking and insurance and 18,257 for accountancy and actuarial work – only 8,042 specified insurance.

A Milkround spokesman says that investment banking institutions tend to attract far more applicants due to the higher salaries and the perception that the ambitious are being offered opportunities.

He adds: "Insurance firms need to shed their stereotypical dowdy image by recruiting more graduates and launching graduate schemes."

Same rewards

The spokesman says insurance companies could also draw attention to the rewards available. "They tend to offer many of the same rewards as banking, but people don't realise this. More could be done to market this fact to encourage more interest towards careers in insurance.

"Banking firms do an incredibly good job promoting their grad schemes, helped by the starting salaries they offer, so they're always massively over-subscribed."

The starting salary for graduates at insurance firms tend to average around £22,000 at the very top firms, but it can be a lot lower, Milkround's statistics show. Accountancy firms tend to pay slightly more on average, at about £25,000. Investment banks offer the top salaries which average £36,000.

Big players in insurance that have had a presence on Milkround include AIG, Allianz, Aon, Aspen Re, AXA, Groupama, Marsh, Miller Insurance, Norwich Union, Saga and Zurich.

➔ graduates rate their career options, these benefits will have to be advertised more widely – something the CII has recognised with the recent launch of its Talent Initiative.

But for the small high street broker, offering such temptations is simply not an option, and the idea of luring graduates away from investment banks is laughable. They have to take another route – grow their own talent.

Recruit locally

Andrews, who used to be head of the CII's insurance faculty before joining Towergate, says: "Unfortunately, there was a time when the smaller broker would recruit well-trained people from insurance companies in their local areas. But as big insurers have withdrawn from many locations over the years, the talent pool has dried up for smaller brokers."

She adds: "Now smaller brokers have to train talent from the roots up, perhaps to a degree they never had to before.

"It will be a struggle. particularly when they have to balance doing business with the regulatory demands on them, plus training, which they have to constantly keep on top of. It is an endless process to train people."

It may be tough to train people, but with commitment and determination it can be done.

Recruitment by numbers

- The UK insurance industry is worth £300bn and is the UK's second largest export
- The sector employs over 330,000 people in a diverse range of roles
- Nearly 90% of graduates will not consider a role in insurance
- 75% of recruiters in the industry struggle to attract quality talent
- Up until a year ago over 70% of industry practitioners did not give information to careers staff
- 80% did not give university campus presentations
- Only a quarter of managing agents had graduate programmes
- The investment banking sector spends just under £4,000 on each recruit, while insurance companies spend just £714.

Manor Insurance is a six-man firm based in Hastings. Managing director Ian Mantel admits: "Retention isn't hard but recruiting isn't easy either. The difficulty for us is that Hastings is quite a depressed town, which means expectations aren't as high among school leavers.

"We don't target graduates as the nearest university is 30 miles away. The applicants we see are predominantly with GCSEs. A few have worked at the local call centre. We also find that university graduates are not prepared to work for small salaries, so they end up working in the City."

But Mantel ensures that his staff receive the training that they need. Staff are encouraged to sit for the CII exams, funded by the company. "Within the office, we use the CII-Biba collaboration, Broker Access, which is ideal for the small broker. It helps us prove our competency to the FSA."

His staff also attend Biba training days held at Bevis Marks or insurers' offices in the City.

Poaching is another option. On a larger scale, with a staff of 80, the Suffolk-based Davis Group recruits most of its staff from other insurance companies.

But according to its human resource and marketing director Henrietta Flynn, this is because it is right on the doorstep of insurers like AXA, Norwich Union and Prudential.

"Insurers provide very detailed training. When people come to us from a broking firm, they have been trained using a more broad-based approach and may not focus on why regulation is useful and necessary," Flynn explains.

> Smaller brokers have to train talent from the roots up, perhaps to a degree they never had to before. It will be a struggle
> Fiona Andrews, Towergate

In companies of any size, succession plans play an important role in retaining employees once they are trained.

Andrews advises brokers to use a competency model, like the CII competency framework, to benchmark knowledge and skills people should have.

This is so they know when to improve and learn to do the next job role. That in itself creates succession feed and gives people a reason to work hard, and to stay in the job.

Whether people come from the local high school or a redbrick university, they are all looking for that motivation.

The driver for this is knowing they are working in a worthwhile and interesting industry and for an employer who cares about and is willing to invest in their career. Every broker, from the biggest to the smallest, can provide that. **IT**

Banking is proving to be the most attractive career proposition for graduates

What the industry has to offer

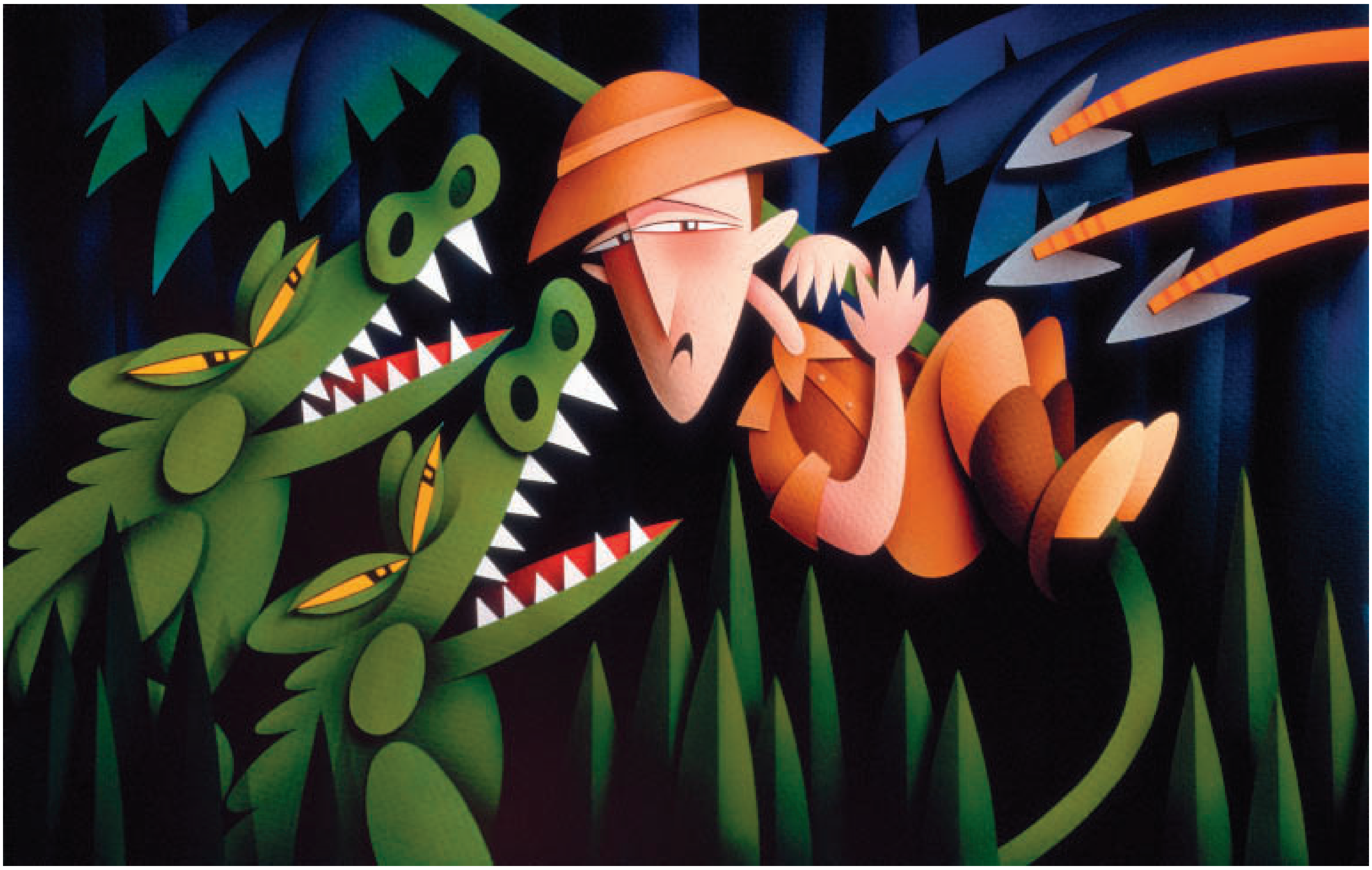
Insurance firms have a real opportunity to make candidates aware that some of the benefits of a banking career can be found in their industry. Similar rewards offered by banking and insurance are:

- Working with big investment funds – learning and applying investment strategies
- Possibly working with dynamic big-name clients
- Good financial rewards – probably not during initial training, but after qualification
- Undergoing rigorous training and exams leading to qualifications which afford status, career advance and monetary rewards
- Often City-based, it come with a good social life
- Possible advantage over banking: much fewer working hours and less stress.

Data from: Milkround.com

Adapt or die

Brokers are facing a multiplication of threats in an ever-changing market. How can they survive? Ellen Bennett explains



Tim Wilson summarises the mood in the market: "These are the toughest times for brokers that I can remember. It's been a soft market now for two or three years, with internecine fighting within the market."

Wilson, sales and marketing director of Close Premium Finance, adds: "SME is very crowded, premiums are at an historic low – brokers are very squeezed at the moment and it's hard to make a living."

It's a gloomy assessment, but arguably a fair one. Brokers face unprecedented competition on all fronts, from direct providers eyeing commercial lines to the booming aggregators and behemoth consolidators swallowing vast chunks of business. So how can the smaller or medium sized business defend itself?

Of course, competition is nothing new. "Brokers have been living in a competitive environment for many years," says Eric Galbraith, Biba chief executive. "We have always seen threats from other channels of distribution coming in and commoditising insurance products, or accessing our customers in different ways."

But the multiplication of threats, and the new forms of communication which make it easier to access the customer, mean that brokers cannot afford to be complacent. A recent survey by Insurecom found that 56% of leading broker respondents described the future of the industry as "adapt or die".

As well as consolidators, brokers were concerned about changing business models, including the growth of direct insurers, and the total absence of customer loyalty.

Regulation was also a concern, with three-quarters of respondents worried about complying with FSA rules. Add to this the worries about business inefficiencies and the challenge of new technology, and it seems a lot of brokers must be having a lot of sleepless nights.

> 'Customers are better informed about where they can go, and what the differences between different distributors are'
> Tim Ablett, consultant

"A few years ago, the whole of the competition was between brokers and insurers," says Tim Ablett, a consultant to Project Consulting Partners.

"But with supermarkets coming more into distribution, and the internet, particularly in personal lines but now increasingly in commercial lines too, there is a new, multichannel competition.

"There has also been a change in the attitudes of customers – before, they saw themselves as the customer of the broker, whereas now they are slightly more promiscuous, and they are better informed about where they can go, and what the differences between different distributors are."

But the market is adaptable, and there are as many ways of responding as there are challenges. ➔

Insurance Times maps out five routes to propel your business into the future.

Survival strategies

1. Sell a stake to an insurer
With insurers such as Norwich Union and Allianz in the market to buy, there can be few brokers out there that have not felt tempted to sell a stake in their business. Though this may raise concerns over independence, it provides much-needed cash for development, and a strong relationship with a key player.
"I would be lying if I said it hasn't crossed my mind," admits Lyndon Wood, chairman of Moorhouse, though he has no current plans to sell. "That's the nature of the business world. We have our own frustrations – we want to quadruple the size of the business, but we need financial backing.
"The simplest solution seems to be to sell part of your business to an insurance company – they have the deepest pockets."

2. Join a network
"If I were running my own company now – bearing in mind all the pressure from consolidators – I would look seriously at network membership," says Tim Wilson, sales and marketing director at Close Premium Finance, and a broker himself for 20 years. "Networks provide the ability to maintain your independence and, for proprietors that are reaching 55 or so and have no obvious succession, it provides an obvious buyer three or four years down the road." As well as these benefits, membership of a network gives a smaller business some of the purchasing power of an organisation many times its size, and other forms of support, such as advice on compliance and documentation. The main networks, such as Broker Network and Cobra, are rapidly increasing in size as brokers join up, seeing them as a means to retain independence in the face of the consolidators.

3. Promote your 'unique selling point'
Biba chief executive Eric Galbraith says: "There is huge competition out there, but brokers are able to differentiate themselves by providing advice and service. Brokers are responding, and have always responded, to the competitive environment they live in." As Galbraith notes, direct providers and internet aggregators share one major flaw: they cannot offer advice. For commercial lines in particular, insurance remains a complicated product which the average client needs unbiased help to understand and select. Only the broker is able to provide this help. So broking businesses should be shouting about the unique service they offer, and ensuring the general public understands the value of advice, as well as price.
This is particularly important when so much marketing is focused on cut-price insurance. The public is being educated to think of insurance as a cheap product, and perhaps to forget the importance of comprehensive cover and top quality service.

4. Specialise
As the Aons and Willises of this world increasingly dominate the general market, smaller providers may find the best way to defend their business is to specialise. The big boys are less likely to be interested in niche work, and customers in these areas tend to be more loyal. For example, a stamp collector would far rather talk to a fellow enthusiast about the value of this collection than a faceless voice from a call centre. Schemes are also becoming a more common, and effective, way of capturing niche business. A small broker can extend its reach well beyond its local area with a good, niche scheme – and underwriters are keen to get on board.

5. Join the technology revolution
"If you can't beat 'em, join 'em," is an old saying, but remains relevant to today's broker. Rather than running scared in the opposite direction of internet aggregators, brokers should embrace the technology they have pioneered and use it to their own advantage – as many are beginning to do. If a client finds it convenient to compare the price of several policies on one site, then how much more convenient would he find it to compare price and cover? Every broker, from the major players to the high street family outfit, should have a modern, comprehensive and easy-to-use website. As well as threats, the internet offers a wealth of opportunities, particularly to businesses outside major cities, which need no longer be constrained by their geographical location.

Why are brokers not being well served?

Brokers believe they receive a poor service from insurers, but who is to blame? Andrew Holt reports

Is it a surprise that insurers' service to brokers is poor? You would think that it's in the interest of insurers to offer good service to brokers, which are essentially a client and can offer more business potential. But poor insurer service is a recurring problem brokers say.

Graham Gibson, Groupama's claims director, was involved in CII research dealing with insurer claims service that found the same trend. "It [insurer service] was shown to be truly awful," says Gibson.

But hang on, don't brokers have a responsibility to demand a better service? Of course they do," says Nick Stanton, head of UK and global carrier management at Aon. "But we don't want to throw rocks over the fence. Dialogue needs to be constructive."

According to Stanton, brokers have as much a responsibility as an insurer to ensure a good service is delivered. "It takes two to tango. There is no benefit in brokers just slagging off insurers' service, we need to work together."

Determining factor

But there is the problem of the price that broker clients demand. "Brokers could make a stance, but then they would have to persuade their clients on price, which is always difficult. Price should not always be the determining factor for brokers, but it often is," says Clive Nathan, Towergate's chief executive of underwriting.

Groupama is a broker-only insurer, and knows the importance of maintaining a good broker service.

"If we did not offer a really good service to our brokers then they would lose clients, they would go elsewhere and we wouldn't have a business," says Gibson.

So what can brokers do? Gibson says that brokers must stand firm. "Brokers need to take a stance and demand they will take their business to other insurers if they do not get a good service. The problem is that price gets in the way, and brokers often place their business on price."

He says brokers are therefore dealing with the situation themselves. "What is already happening is that brokers are dealing with claims because they are fed up with the insurers' claims service, and using outsourced claims companies.

Photo courtesy BBC

"If this continues it will be to the detriment of insurers and they have only themselves to blame."

Are insurers realising this, and improving? Stanton says yes. "What has changed is that service is more on their senior management's agenda than it ever has been. Years ago it was about cutting costs, now it is about better service. That is a major change and a good one."

The biggest issue is how claims are dealt with. "Claims are the main piece, because it is what insurers are selling. Being effective with policies and getting documents out accurately is vital," says Stanton.

Gibson adds: "Being effective and efficient in your claims service should not be too much to ask."

If insurers didn't regularly make a mess a policy documentation, brokers wouldn't be besieging their phone , he says.

Another broker says: "Claims handling has deteriorated significantly across the board. This puts a strain on the best relationship."

But it's the availability of quality staff that counts, says Gibson. "The demand for technical staff will increase, despite the fact that it is already difficult to get good technical staff, and certain claims jobs are being dumbed down," he says.

Towergate's Nathan says: "Insurers are very good when it come to the plain vanilla areas, but when it comes to more complex issues they fall far short."

Groupama's Gibson says that offshore call centres have much to answer for. "I am not having a go at individual insurers, but if you have a call centre in the back of beyond which does not know our culture you are not going to get the empathy that clients need."

And does size matter? "I think it does," says Aon's Stanton. "Usually, smaller firms are better at service than bigger companies because of their more personal approach."

Nathan adds: "Good service costs money, and many insurers have typically looked to cut costs. That is changing, but slowly."

> 'Brokers are dealing with claims because they are fed up with the insurers' claims service'
>
> Graham Gibson, Groupama

Anecdotally, brokers are rewarding insurers with extra business if they can provide some kind of field underwriter service .

Another issue is that of insurer staffing – both in quality and quantity. Many brokers highlight the sheer difficulty and waste of time in getting through to their insurers. Not surprisingly offshore call centres are despised the most.

One broker sums it up: "We're all fed up with pressing one for this and two for that and listening to your tinny music and assurance that our call is important to you. If it was that important, you would have enough people on hand to answer it."

Decision-making

Getting through is of little help of course if the person on the other end is clueless. Too often, it seems, brokers find themselves unable to reach anyone with decision-making ability.

Most major insurers do not have sufficient resources, which results in service levels varying between poor, at best, and dreadful," says another broker.

Brokers are not happy about the level of centralisation and bureaucracy in today's large composite insurers. The feeling seems to be that it doesn't fit their business model. To their clients, a broker exists for advice, to negotiate suitable cover at a competitive price and to ensure that any claims are paid promptly.

Yet with the larger insurers, brokers are seemingly struggling to achieve any meaningful personal contact or influence. Some brokers are forming the impression that certain insurers see them not as partners, but as a set of middlemen to be tolerated only until all business can be brought direct or through a few favoured brokers.

Summing up the feelings of many, the broker adds: "The problem is that personal relationships are not made between insurer staff and broker staff. On many occasions, you do not really know who you should be talking to. Also many underwriters do not fully understand risk, probably due to lack of training.

"Gone are the days when you could pick up the phone and discuss an aspect of a policy and ask to be flexible or creative in their approach." IT