A revolution will soon transform conflicts of interest in insurance

By Duncan Minty 30th January 2018

Conflicts of interest have been so common in insurance, and for so long, that the sector sometimes struggles to pay them enough attention. Some arrangements must still cause a regulatory eyebrow to shoot up in amazement. They persist, tucked away in the myriad of deals that abound in such an intermediated market.

Not for much longer though. A revolution is about to transform conflicts of interest in insurance, and brokers and insurers alike must be prepared for the repercussions.

Conflicts of interest are here to stay. The revolution I'm referring to isn't going to sweep them out of the market. That would be impossible, for they permeate the market, from claims through to broking. What this revolution will do is shine a very bright light on them. It will allow conflicts of interest in insurance markets to be identified and weighed up with little more than some clever software and a click of a mouse.

Transparency and Risk

So the question brokers and insurers need to ask themselves is this. Are all of your deals, facilities, delegated authorities and schemes structured in such a way that you'd be happy for them to appear on the front page of the Wall Street Journal? This is a classic ethics test, centred around the transparency that this revolution will soon deliver. And if you weren't happy to see them so exposed, what risks does that pose to your business, to your career?

Take the £4m fine handed out in December 2017 to the UK insurance broker Bluefin (more here). The regulator found that they had failed to deal with the conflicts of interest inherent in the relationship with their then owner AXA. Yet this fine was for events between 2011 and 2014. This is oversight through a regulatory rear view mirror. The revolution that's coming will consign that rear view mirror to the bin. In its place will be a real time window into the day to day arrangements at the heart of how the market works.

The Power behind the Revolution

This real time window will be powered by artificial intelligence and utilise an array of tools to map business relationships and network flows. One tool already being used in various forms of enforcement is social network analysis (SNA). It allows social structures at both the individual and corporate levels to be analysed, and patterns and concentrations identified.

This is an example of 'SupTech': the use of technology for supervisory purposes. And brokers, insurers and MGAs need to keep a watch on how it develops, for it allows a regulator to do things they've never been able to do before. Combine SupTech with the individual accountability at the heart of regulatory initiatives like the UK's Senior Manager and Certification Regime, and there is the revolution.

One benchmark that market players can use to measure the imminence of tools like SNA being applied to their business can be found in insurance fraud. SNA is being used to identify the networks responsible for organised insurance fraud. Its prevalence there is an indicator of its availability as a regulator tool for tackling conflicts of interest.

SNA will feed on the data about all those flows of business around the market. Alongside it, other SupTech tools will analyse the communications associated with all that business. These could be 'one-to-many', in the form of digital marketing, or 'one-to-one', in the form of client communications. This is already happening and enables questions to be asked about whether the message about the deal matches the substance of the deal.

The Momentum behind SupTech

Now, you may ask where the momentum behind SupTech is coming from. Here are three factors. Firstly, there's a danger that a digitising market could get beyond regulatory reach, unless the regulators digitised their act too. Secondly, getting left behind in this way makes the likelihood of another big mis-selling scandal even greater. That is something regulators are determined not to face again. And thirdly, a digitising market is likely to change the shape and nature of intermediation. If this is not understood by the insurance buying public, all sorts of market confidence issues could emerge.

Two wider points are worth noting. Firstly, firms shouldn't think that they're small enough to slip under that SupTech radar. The opposite is true: every firm produces data that SupTech feeds upon. And secondly, this revolution will reopen a debate about what it means to be independent, about how a client's interests are best served, perhaps even about the very nature of agency itself. The market needs to be prepared for such a debate.

What they can also do to prepare for this SupTech revolution is...

- revisit their own conflict of interest risk assessment and use the outputs to identify where the main problems lie;
- if the firm's business arrangements are numerous and complex, use social network analysis itself to identify where the main exposures lie. It's not rocket science and if need be, can be done at first node level on paper;
- apply some critical thinking to the firm's stance on conflicts of interest. Is the culture right? Do leaders understand the implications? Have we applying mitigation properly?

Remember: the ethics of conflicts of interest in insurance lie not so much in their existence, but in how you handle them. That's a question SupTech will force firms to take very seriously