

SHORT-TERM INSURANCE ACT

REQUEST FOR COMMENTS: DRAFT AMENDMENTS TO THE REGULATIONS MADE UNDER SECTION 70 TO BE PROPOSED TO THE MINISTER OF FINANCE (BINDER AGREEMENTS)

The Registrar of Short-term Insurance wishes to propose the amendment of the regulations issued under the Short-term Insurance Act, 1998 (Act No. 53 of 1998), as set out in Schedule A hereto, to the Minister of Finance for consideration and, if the Minister agrees therewith, promulgation under section 70 read with section 48A of the Short-term Insurance Act, 1998.

An explanatory memorandum on the proposed draft amendment of the regulations is set out in Schedule B hereto.

All interested persons are invited to make representations on the proposed amendment of the regulations. Comments on the proposed amendment of the regulations may be submitted in writing on or before 31 October 2010 to the Registrar of Short-term Insurance per email to STBinders@fsb.co.za.

The proposed draft amendment of the regulations is available on the Financial Services Board's web site at <http://www.fsb.co.za>.

Registrar of Short-term Insurance

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SCHEDULE A

1. Substitution of Part 6 in the Regulations under the Short-term Insurance Act, 1998 as published in GN R1493 of 1998 and amended by GN R462 of 2008

The following Part is hereby substituted for Part 6 of the Regulations:

“PART 6

BINDER AGREEMENTS

Definitions and interpretation

6.1 (1) In this Part 6, unless the context indicates otherwise –

“**associate**” has the meaning assigned to it in the General Code;

“**binder agreement**” means an agreement contemplated in section 48A;

“**binder holder**” means a person with whom an insurer has concluded a binder agreement;

“**commercial lines business**” means short-term insurance business in respect of which the policyholder is a legal person;

“**enter into**” means any act that results in an insurer becoming liable to provide policy benefits under a policy where that insurer becomes aware of such liability only after it has arisen;

“**General Code**” means the General Code of Conduct for Authorised Financial Services Providers and Representatives as published in Board Notice No. 80 of 2003, and amended from time to time, under section 15 of the Financial Advisory and Intermediary Services Act, 2002 (Act No. 37 of 2002);

“**insurer**” means a short-term insurer or a Lloyds underwriter;

“**mandated intermediary**” means an independent intermediary that holds a written mandate from a potential policyholder or policyholder that authorises that intermediary, without having to obtain the prior approval of that potential policyholder or policyholder, to –

- (a) terminate the policy of that policyholder; or
- (b) perform any act, in relation to a policy, that legally binds that potential policyholder or policyholder;

“**non-mandated intermediary**” means a representative or an independent intermediary, other than a mandated intermediary;

“**policy**” means a short-term policy;

“**renew**” means any act that results in the renewal of an insurer’s liability to provide policy benefits under a policy where that insurer becomes aware of the renewal of liability only after it has arisen;

“**representative**” has the meaning assigned to it in the Act, but excludes an employee of an insurer;

“**settle claim**” means to –

- (a) accept a claim for policy benefits or a part thereof;

- (b) determine the liability of an insurer under a claim for policy benefits; or
- (c) reject or refuse to pay a claim for policy benefits or a part thereof;

“**this Part**” means this Part 6; and

“**underwriting manager**” means a person (other than an independent intermediary, an associate of an independent intermediary or a representative) that renders a service to an insurer only;

“**vary**” means any act that results in the variation, termination, repudiation or denial of an insurer’s liability to provide policy benefits under a policy where that insurer becomes aware of that variation, termination, repudiation or denial of liability only after it has arisen, and includes any act declaring a policy void;

(2) An underwriting manager who is a binder holder in respect of certain types or kinds of policies of an insurer cannot also be a binder holder for another insurer in respect of the same types or kinds of policies.

Requirements, limitations and prohibitions relating to binder agreements

6.2 (1) An insurer, subject to regulation 6.4, may have a binder agreement with only one or more of the following persons -

- (a) a non-mandated intermediary that is not an associate of a mandated intermediary; or
- (b) an underwriting manager.

(2) A binder agreement must, in addition to those matters provided for under section 48A(2) -

- (a) specify the duration of the agreement;
- (b) specify the level and standard of service that must be rendered to a policyholder, where relevant, and to the insurer;
- (c) require that the binder holder has appropriate management systems, risk management systems and information technology systems in place to render the services under the binder agreement;
- (d) specify the Rand value of the remuneration or consideration contemplated under regulation 6.3 payable by the insurer to the binder holder in respect of each policy and generally, or, if the Rand value is not fixed or determinable on entering into the agreement, the basis on which the remuneration or consideration payable will be calculated;
- (e) specify the disclosures that must be made and the information that must be provided to a policyholder, and the manner in which such disclosures or information must be made or provided when a binder holder –
 - (i) enters into, varies or renews a policy;
 - (ii) determines the wording of a policy;
 - (iii) determines premiums under a policy;
 - (iv) determines the value of policy benefits under a policy; or
 - (v) settles a claim under a policy;

- (f) provide for the type and frequency of reporting by the binder holder on the services rendered under the binder agreement;
 - (g) provide for the manner in and the means by which an insurer must monitor the binder holder's performance under and compliance with the binder agreement;
 - (h) provide for periodic performance reviews of the binder holder and the regular review of the binder agreement;
 - (i) specify that the insurer has continued access to policyholder and policy information held by the binder holder;
 - (j) provide for the intervals, which may not be longer than 60 days, at which the binder holder will update policyholder and policy information in the records of the insurer, which information must, at least, enable the insurer to identify the policyholders, contact the policyholders and assess its liability under the policies;
 - (k) set out any warranties or guarantees to be furnished and insurance to be secured by the binder holder in respect of its ability to fulfill its contractual obligations;
 - (l) provide for a dispute resolution process;
 - (m) provide for a termination period, irrespective of the circumstances under which the agreement is terminated, of at least 90 days, that will allow –
 - (i) the binder holder and insurer to comply with any legislative requirements relating to the policies referred to in the binder agreement; and
 - (ii) for the transfer or sharing of all electronic and paper-based records in respect of the policies referred to in the binder agreement, including the names and identity numbers of all policyholders, insured persons and beneficiaries; and
 - (n) provide for the continuity of service if the binder holder is placed under curatorship, business rescue, becomes insolvent, is liquidated or is for any reason unable to continue to render the services in accordance with the binder agreement.
- (3) (a) A binder agreement may only provide for matters referred to in section 48A of the Act, this Part and matters incidental thereto, and may not regulate any other arrangement or relationship with the binder holder, irrespective of such other arrangement or relationship being dependent on the conclusion of a binder agreement or that the binder agreement is in addition to or consequential on such other arrangement or relationship.
- (b) A binder agreement may not prohibit an insurer from communicating directly with any independent intermediary or its policyholder.
- (4) A binder agreement concluded with a non-mandated intermediary, in addition to the matters provided for under sub-regulation (2), must limit the discretion of the binder holder in respect of -
- (a) the maximum value of policy benefits that may be determined under each policy or the maximum value of any claim that may be settled by the binder holder under the policies to which the binder agreement relates;
 - (b) the risk factors that must be considered by the binder holder when entering into, varying or renewing a policy or determining the value of policy benefits under a policy;

(c) other parameters in accordance with which the binder holder must render the services provided for in the binder agreement.

(5) A binder agreement concluded with a non-mandated intermediary may not authorise the binder holder to –

- (a) refuse to renew a policy;
- (b) reject or refuse to pay a claim for policy benefits or a part thereof;
- (c) terminate, repudiate or deny an insurer's liability to provide policy benefits under a policy; or
- (d) declare a policy void.

Requirements, limitations and prohibitions relating to any consideration that may be offered or provided to a binder holder, and any participation by a binder holder in profits attributable to the policies referred to in a binder agreement

6.3 (1) An insurer may pay a binder holder a fee for the services rendered under the binder agreement, which fee must be reasonably commensurate with the actual costs of the binder holder associated with rendering the services under the binder agreement, with allowance for a reasonable rate of return for the binder holder.

(2) Any fee referred to under sub-regulation (1) payable to a non-mandated intermediary that may settle claims or determine the value of policy benefits under a binder agreement, may not constitute or be based on a percentage of the difference between an amount claimed or the maximum value of policy benefits payable under a policy and the policy benefits actually provided to a policyholder in settlement of a claim.

(3) A non-mandated intermediary that is a binder holder, in respect of the services rendered under the binder agreement, may not directly or indirectly receive or be offered any share in the profits of the insurer attributable to the type or kind of policies referred to in the binder agreement.

(4) An underwriting manager, in respect of the services rendered under the binder agreement, may share in the profits of the insurer attributable to the type or kind of policies referred to in the binder agreement.

(5) Any fee referred to under this regulation 6.3, payable to a non-mandated intermediary that is a binder holder must be disclosed to a policyholder, which disclosure must be included in the disclosures contemplated under regulation 6.2(2)(e).

Exemption

6.4 (1) Despite regulation 6.2(1), -

- (a) an insurer may conclude a hold-covered binder agreement with a mandated intermediary or a non-mandated intermediary, if –
 - (i) that agreement provides for the entering into policies on an interim and limited-in-time basis only; and
 - (ii) the legal liability of the insurer under such policies lapses after a maximum period of 96 hours in respect of personal lines business and 30 days in respect of commercial lines business, unless the insurer, in respect of each policy, confirms its legal liability under that policy in writing prior to the expiry of such period; and

- (iii) no fee for the services rendered under the hold-covered binder agreement is payable to the mandated intermediary or non-mandated intermediary by the insurer; and
- (b) an insurer may conclude a binder agreement with –
 - (i) a non-mandated intermediary in respect of commercial lines business that is also a mandated intermediary in respect of personal lines business, but not in respect of that commercial lines business; or
 - (ii) a non-mandated intermediary in respect of personal lines business that is also a mandated intermediary in respect of commercial lines business, but not in respect of that personal lines business.

(2) (a) Regulations 6.2(2)(d) and 6.3 do not apply to a hold-covered binder agreement concluded under sub-regulation (1)(a).

(b) For purposes of a hold-covered binder agreement, the timeframe referred to under regulations 6.2(2)(j) and (m) are 96 hours in respect of personal lines business and 30 days in respect of commercial lines business.

Reporting requirements

6.5 (1) An insurer, within 30 days of giving or receiving notice of the termination of a binder agreement, must inform the Registrar in writing and in the format required by the Registrar-

- (a) of the date on which the binder agreement will terminate;
- (b) of the reasons for the termination of the binder agreement;
- (c) how the policies to which the binder agreement relates will be dealt with;
- (d) how any legislative requirements relating to the termination of the binder agreement or policies, if one or more policies to which the binder agreement relates will be terminated, will be complied with.

Transitional arrangements

6.6 (1) Any agreement referred to under section 48 of the Act concluded before or on the date on which this Part commences must be aligned with this Part within one year of this Part coming into operation.”

2. Insertion of Part 7 in the Regulations under the Short-term Insurance Act, 1998 as published in GN R1493 of 1998 and amended by GN R462 of 2008

Part 7 is hereby inserted after Part 6 of the Regulations:

“PART 7 TITLE AND COMMENCEMENT

7.1 These regulations shall be known as the Regulations under the Short-term Insurance Act, 1998.

7.2 (1) Regulations 1 to 5, other than regulation 4.2, came into operation on commencement of the Act. Regulation 4.2 came into operation on 25 April 2008.

(2) Regulation 6 came into operation on [*insert date*].

(3) Any amendments to regulations 1 to 6 come into operation on the date of publication thereof in the *Government Gazette* or on such other date specified by the Minister in the *Government Gazette* or specified in a regulation.”

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SCHEDULE B
EXPLANATORY MEMORANDUM

1. PURPOSE

The purpose of this Explanatory Memorandum is to provide insight into the principles that informed the draft regulations and explain how these principles are reflected in the draft regulations.

2. BACKGROUND

The enhancement of the legislative framework relating to binder agreements commenced with the enactment of the Insurance Laws Amendment Act No. 27 of 2008.

The latter Act amended the existing provisions of the Short-term Insurance Act and introduced provisions in the Long-term Insurance Act relating to binder agreements. Before the enactment of the latter Act, binder agreements in the long-term insurance industry were not regulated.

The Short-term Insurance and Long-term Insurance Acts, as amended (the Insurance Laws), afford the Minister of Finance legislative authority to make regulations on a number of matters relating to binder agreements.

Subsequent to the enactment of the Insurance Laws Amendment Act, a Binder Task Team with representation from the National Treasury, the Financial Services Board and industry associations (ASISA, SAIA, FIA and SAUMA) was constituted. The mandate of the Binder Task Team was to draft binder regulations for consideration by the Minister of Finance. In addition, the Financial Services Board met separately with industry associations to discuss the potential impact of binder regulations on the long-term and short-term insurance industries.

The draft binder regulations are therefore the result of robust and inclusive consultation with interested and affected stakeholders.

3. SCOPE OF THE DRAFT REGULATIONS

The draft regulations represent but one of a series of initiatives and projects of the National Government and the Financial Services Board.

The draft regulations therefore do not address the following aspects, which are the subject of separate processes, –

- 3.1 the issues relating to intermediary relationships raised in the Contractual Savings Discussion Document;
- 3.2 the outsourcing of core insurer functions to third parties holistically. The draft regulations only address a subset of outsourcing namely the outsourcing of binder functions;
- 3.3 ownership structures or cell arrangements, in particular conflicts of interests that are inherent in these structures and arrangements.

Binder functions are the collective term used for those functions that a binder holder performs as the agent of the insurer. The binder holder acts on behalf of the insurer, as if the binder holder is the insurer, when interacting with potential policyholders and policyholders.

4. RELEVANT ACTS AND THE DRAFT REGULATIONS

- 4.1 **The Short-term Insurance Act:** The Short-term Insurance Act (the Act) contains the fundamental policy or underlying principles relating to binders. It provides for the basic or minimum issues and powers necessary to regulate binders and delegates legislative (law-making) and other authority to implement and enforce the Act to the Minister of Finance.

The draft regulations are the detailed regulation of matters provided for in the Act. They supplement the Act by prescribing detailed and technical rules.

The draft regulations must be read with the Act.

The relevant extract from the Act (section 48A) is included at the end of this Schedule as Annexure 1.

- 4.2 **The Financial Advisory and Intermediary Services Act:** The draft regulations refer to the Financial Advisory and Intermediary Services Act. This is so to, in as far as reasonably possible, ensure consistency in respect of terminology used and to avoid any interpretation difficulties that may arise in implementing the draft regulations.

The draft regulations must therefore also be read with the latter Act.

5. BROAD PRINCIPLES THAT INFORMED THE DRAFT REGULATIONS

The following broad principles informed the draft regulations:

- 5.1 **Accountability of the insurer:** The insurer is responsible for complying with the Act, irrespective of the fact that the insurer outsources some of its functions to a third party.
- 5.2 **Responsible outsourcing:** Where an insurer outsources “binder functions” to a third party, the insurer must ensure that the contractual arrangements, and the oversight and management of the contractual arrangements, facilitate (not impede) the insurer’s compliance with the Act and the fair treatment of policyholders.
- 5.3 **Policyholder protection:** Policyholder interests and the fair treatment of policyholders may not be prejudiced by the outsourcing of “binder functions” by an insurer.
- 5.4 **Conflicts of interest:** Any potential conflicts of interest that may arise where a non-mandated intermediary is a binder holder must be avoided.

6. SUMMARY OF THE DRAFT REGULATIONS

6.1 Who may be a binder holder?

[See regulations 6.2(1)]

An underwriting manager or a non-mandated intermediary may be a binder holder.

Underwriting manager

[See regulations 6.1 and 6.2(1)]

An underwriting manager is defined in the draft regulations as a person (other than an independent intermediary¹, an associate² of an independent intermediary or a representative³) that renders a

¹ A list of relevant definitions is included at the end of this Schedule as Annexure 2.

² A list of relevant definitions is included at the end of this Schedule as Annexure 2.

³ A list of relevant definitions is included at the end of this Schedule as Annexure 2.

service to an insurer only.

The person therefore acts as the agent of the insurer (i.e. as if that person is the insurer) and does not act on behalf of a policyholder, potential policyholder or an independent intermediary. The person also therefore does not intermediate between a policyholder or a potential policyholder and the insurer, i.e. the person does not render services as an intermediary⁴ as defined in the Act.

An underwriting manager who is a binder holder in respect of certain types or kinds of policies of an insurer cannot also be a binder holder for another insurer in respect of the same types or kinds of policies.

Non-mandated intermediary

[See regulations 6.1 and 6.2(1)]

A non-mandated intermediary is defined in the draft regulations as a representative or an independent intermediary that *does not* hold a written mandate from a potential policyholder or policyholder that authorises that intermediary (without having to obtain the prior approval of that potential policyholder or policyholder) to terminate the policy of that policyholder or perform any act, in relation to a policy, that legally binds that potential policyholder or policyholder.

By contrast, a mandated intermediary is an independent intermediary that has a written mandate from a potential policyholder or policyholder to move a policy or “book of business” to another insurer without having to secure the prior approval of the policyholder or all policyholders.

This means that a non-mandated intermediary may be a binder holder, but is not permitted to move a policy or “book of business” to another insurer, unless the non-mandated intermediary has, in respect of each move, –

- expressly secured the prior written approval of each policyholder or complied with section 36 of the Act; and
- met the requirements relating to replacement products as set out in section 8 of the General Code of Conduct for Authorised Financial Services Providers and Representatives⁵.

In order to limit potential conflicts of interest, a non-mandated intermediary that is a binder holder cannot simultaneously be a mandated intermediary, nor may it be an associate of a mandated intermediary. However, certain exemptions are granted in this regard (see the discussion on exemptions immediately below). What constitutes an associate is defined in the draft regulations with reference to the definition of this term in the Code of Conduct for Authorised Financial Services Providers and Representatives.

As to the use of the term “writing”, please note that the Electronic Communications and Transactions Act No. 25 of 2002, in section 12, provides that a requirement in law that a document or information must be in writing is met if the document or information is in the form of a data message and accessible in a manner usable for subsequent reference.

A non-mandated intermediary may be a binder holder for all types of business or just some, but this must be expressly specified in the binder agreement.

Exemptions

[See regulation 6.4 and paragraph 5.5 below]

⁴ A list of relevant definitions is included at the end of this Schedule as Annexure 2.

⁵ The General Code of Conduct for Authorised Financial Services Providers and Representatives as published in Board Notice No. 80 of 2003, and amended from time to time, under section 15 of the Financial Advisory and Intermediary Services Act No. 37 of 2002.

Certain exemptions from the general rule of who may be binder holders as explained above are provided for in the draft regulations.

The draft regulations allow an insurer to conclude a hold-covered binder agreement with a mandated intermediary or a non-mandated intermediary under certain specific circumstances. Some of the requirements of the draft regulations in respect of consideration and matters to be included in the agreement do not apply to hold-covered binder agreements.

The draft regulations also allow an insurer to conclude a binder agreement with –

- a non-mandated intermediary in respect of commercial lines business where that intermediary is also a mandated intermediary in respect of personal lines business (but not that commercial lines business); or
- a non-mandated intermediary in respect of personal lines business where that intermediary is also a mandated intermediary in respect of commercial lines business (but not that personal lines business).

6.2 What may a binder holder do and not do on behalf of an insurer?

Definitions

[See regulation 6.1]

The Act allows an insurer, in terms of a written agreement and in accordance with any requirements, limitations or prohibitions that may be prescribed by regulation, to allow another person to do any one or more of the following on behalf of that insurer:

- enter into, vary or renew a policy
- determine the wording of a policy
- determine premiums under a policy
- determine the value of policy benefits under a policy
- settle claims under a policy

The draft regulations define certain of these functions to ensure consistent interpretation. The draft regulations define the following terms “enter into”, “renew”, “vary” and “settle claim”.

General

[See regulation 6.2(2) and (3)]

The draft regulations require binder agreements to include matters in addition to those required by the Act.

The draft regulations further prohibit a binder agreement from regulating any other arrangement or relationship with the binder holder. The draft regulations also state that a binder agreement may not prohibit an insurer from communicating directly with independent intermediaries or its policyholders. These prohibitions on what may be included in a binder agreement are in addition to the prohibitions set out in the Act.

The Act states that a binder agreement may not authorise that other person to add an amount to any gross premium unless the regulations provides otherwise. After consideration of the issue, it was concluded that it would not be appropriate to provide in the regulations for any additions to gross premiums or deductions from claims in respect of policies referred to in binder agreements, as all costs associated with the policy should be determined by the insurer and included in gross premiums.

The draft regulations together with the Act therefore clearly stipulate what a binder holder may and may not do.

A binder holder may not further delegate binder functions. This does not however prohibit a binder holder from outsourcing certain functions that do not fall within the definition of binder functions.

It is important to read the Act together with the draft regulations when drafting or entering into a binder agreement.

Limitations on binder agreements with a non-mandated intermediary

[See regulation 6.2(4) and (5)]

The draft regulations require a binder agreement concluded with a non-mandated intermediary to limit the discretion of the binder holder in respect of -

- the maximum value of policy benefits that may be determined under each policy or the maximum value of each claim that may be settled by the binder holder under the policies to which the binder agreement relates;
- the risk factors that must be considered by the binder holder when entering into, renewing or varying a policy or determining the value of policy benefits under a policy;
- other parameters in accordance with which the binder holder must render the services provided for in the binder agreement.

The draft regulations further prohibit a binder agreement concluded with a non-mandated intermediary from allowing that binder holder to refuse to renew a policy, reject or refuse to pay a claim for policy benefits or a part thereof, terminate, repudiate or deny an insurer's liability to provide policy benefits under a policy, or declare a policy void. This does not affect the ability of a binder holder to settle a claim for an amount less than the amount claimed. It also does not mean that the binder holder may not inform a policyholder that a claim cannot be dealt with until the documents and other information required under the policy have been received.

These additional requirements relating to binder agreements concluded with non-mandated intermediaries are necessary to prevent any potential conflicts of interest that may arise for non-mandated intermediaries when simultaneously acting on behalf of an insurer and a policyholder.

6.3 What must a binder agreement provide for?

[See regulation 6.2(2) to (5)]

As mentioned above, the draft regulations require binder agreements to include matters in addition to those required by the Act and prohibit matters in addition to those prohibited by the Act. Further, specific requirements are provided for binder agreements concluded with non-mandated intermediaries.

In this regard, it must be noted that regulation 6.2(2)(j) that requires a binder agreement to provide for the intervals at which the binder holder must update policyholder and policy information in the records of the insurer does not conflict with the Act that requires a binder holder to make available to the insurer, its statutory actuary, if appointed, and its auditors the policies to which the binder agreement relates and any information relating thereto upon request. The two requirements must be read together. The regulation provides for the regular updating of information and the Act provides for *ad hoc* information requests.

Further, it must be noted that regulation 6.2(2)(m) does not prohibit an insurer from stopping the binder holder from performing certain binder functions or taking steps to mitigate its risks pending the termination of the binder agreement. The minimum 90-day period is necessary to provide for the orderly winding-up of the binder agreement.

6.4 What consideration may a binder holder receive under a binder agreement?

General

[See regulation 6.3]

The draft regulations allow an insurer to pay a binder holder a fee for the services rendered under the binder agreement.

This fee must be reasonably commensurate with the actual costs incurred by the binder holder associated with rendering the services under the binder agreement, with allowance for a reasonable rate of return for the binder holder. This criterion is necessary to deter circumvention of the commission regulations and inappropriate incentives.

The draft regulations do not affect any commission that may be payable to a non-mandated intermediary for rendering services as an intermediary in relation to the policies to which the binder agreement relates or an outsourcing fee payable for outsourced functions performed by the binder holder on behalf of the insurer, provided that –

- the commission regulations are complied with;
- a person / intermediary may not be remunerated for the same or a similar service twice; and
- any remuneration paid is reasonable and commensurate with the actual cost of the services rendered.

The draft regulations also do not affect the ability of a non-mandated intermediary to negotiate a policy fee with the policyholder in terms of section 8(5) of the Act. However it should be noted that the circumstances under which this may occur are under review as the principle is that the policyholder should not be charged twice for the provision of the same or similar service – in particular, the policyholder should not be charged a fee for the provision of a service that falls within the definition of intermediary services for which the intermediary is remunerated by means of commission.

The Financial Services Board is currently developing proposals to clarify the interpretation of the definition of intermediary services for which regulated commission is payable versus outsourced insurer or policyholder services for which a fee may be payable.

Underwriting manager

[See regulation 6.3(1) and (4)]

The draft regulations allow an underwriting manager that is a binder holder to share in the profits of the insurer attributable to the type or kind of policies referred to in the binder agreement.

Non-mandated intermediary

[See regulation 6.3(1), (2), (3) and (5)]

The draft regulations prohibit any fee payable to a non-mandated intermediary that may settle claims or determine the value of policy benefits paid under a binder agreement, from constituting or being based on a percentage of the difference between an amount claimed or the maximum value of policy benefits payable under a policy and the policy benefits actually provided to a policyholder in settlement of a claim. This is necessary to prevent a non-mandated intermediary (that is supposed to act also in the interest of policyholders) from acting in the interest only of the insurer to the detriment of policyholders.

The fee payable to a non-mandated intermediary that is a binder holder must be disclosed to a policyholder.

The draft regulations further prohibit a non-mandated intermediary that is a binder holder from (directly or indirectly) receiving or being offered any share in the profits of the insurer in respect of, specifically, the services rendered under the binder agreement and the type or kind of policies referred to in the binder agreement. This prohibition is therefore not a general prohibition on profit sharing *per se*. It merely prohibits a non-mandated intermediary from being entitled to a percentage of the profits that the intermediary generates because of its performance of the binder functions provided for in the binder agreement. This is again necessary to prevent a non-mandated intermediary (that is supposed to act also in the interest of policyholders) from acting in the interest only of the insurer to the detriment of policyholders.

6.5 Which binder agreements need not meet all the requirements of the draft regulations?

[See paragraph 5.1 above and regulation 6.4]

The draft regulations allow an insurer to conclude a hold-covered binder agreement with a mandated intermediary or a non-mandated intermediary under the following circumstances –

- if the agreement provides for the entering into policies on an interim and limited-in-time basis only; and
- if the legal liability of the insurer under such policies lapses after a maximum period of 96 hours in respect of personal lines business and 30 days in respect of commercial lines business, unless the insurer, in respect of each policy, confirms its legal liability under that policy in writing prior to the expiry of such period; and
- if no fee for the services rendered under the hold-covered binder agreement is payable to the mandated intermediary or non-mandated intermediary by the insurer.

Some of the provisions of the draft regulations on what must be included in a binder agreement and on consideration that may be received or offered do not apply to a hold-covered binder agreement.

6.6 What must an insurer report to the Registrar when a binder agreement will terminate?

[See regulation 6.5]

The draft regulations require an insurer, pending the termination of a binder agreement, to report the following to the Registrar -

- the date on which the binder agreement will terminate;
- the reasons for the termination of the binder agreement;
- how the policies to which the binder agreement relates will be dealt with;
- how any legislative requirements relating to the termination of the binder agreement or policies, if one or more policies to which the binder agreement relates will be terminated, will be complied with.

This is necessary to enable the Registrar to ensure that the termination and consequences of termination are managed in the best interest of the policyholders.

6.7 Must binder agreements entered into prior to the effective date of the draft regulations comply with the draft regulations?

[See regulation 6.6]

Binder agreements concluded before or on the date on which these draft regulations commence must be aligned with the draft regulations within one year of it coming into operation.

7. IMPLICATIONS FOR PARTICULAR PARTIES

The draft regulations will have particular implications for various parties often referred to in industry terms as “administrators”. The term administrator is used broadly to refer to a variety of business models involving a range of administrative services, some of which may fall into the definition of binder functions or intermediary services.

As a binder agreement may only be entered into with a non-mandated intermediary or an underwriting manager, parties currently referred to as administrators wishing to perform binder functions must choose to do so either as:

- a non-mandated intermediary, subject to the limitations on the binder function and policyholder mandate described above; or
- an underwriting manager, defined above as a party acting solely as an agent of the insurer who may not be an independent intermediary or an associate of an independent intermediary.

Administrators providing services that do not fall under either the definition of intermediary services or binder functions may continue to provide these administrative services to an insurer on an outsourced basis without having to be recognised as either an independent intermediary or underwriting manager for the purposes of these regulations.

The Financial Services Board is currently developing a directive and guideline in respect of the outsourcing of services and functions by insurers to ensure that adequate governance, internal controls and risk management are in place in respect of such outsourcing.

8. WHAT ARE THE CONSEQUENCES OF NOT COMPLYING WITH THE ACT AND THE REGULATIONS

The Act, in section 65 read with the definition of “this Act” in section 1, makes non-compliance with section 48A and the regulations issued under section 48A a criminal offence.

Further, the Registrar, under section 6A of the Financial Institutions (Protection of Funds) Act No. 28 of 2001, may refer any non-compliance with the Act or regulations issued thereunder to the enforcement committee established under section 10 of the Financial Services Board Act No. 97 of 1990.

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EXTRACT FROM THE SHORT-TERM INSURANCE ACT: SECTION 48A

Binder agreements

48A. (1) A short-term insurer or a Lloyd's underwriter may, in terms of a written agreement only, and in accordance with any requirements, limitations or prohibitions that may be prescribed by regulation, allow another person to do any one or more of the following on behalf of that insurer:

- (a) enter into, vary or renew a short-term policy, other than a short-term reinsurance policy, on behalf of that insurer or Lloyd's underwriter;
- (b) determine the wording of a short-term policy;
- (c) determine premiums under a short-term policy;
- (d) determine the value of policy benefits under a short-term policy;
- (e) settle claims under a short-term policy.

(2) A written agreement referred to in subsection (1) must—

- (a) set out which of the activities referred to in subsection (1) that other person may perform and the particular kinds of short-term policies in respect of which those activities may be performed;
- (b) set out the particular kinds of short-term policies which may be entered into, varied or renewed by that other person;
- (c) state if that other person is authorised to determine the wording of the policies referred to in paragraph (a), and if authorised, the extent to which and the circumstances under which the wording may be determined;
- (d) state if that other person is authorised to determine premiums in respect of the policies referred to in paragraph (a), and if authorised, the gross premiums of the basis for the calculation of gross premiums that may be determined, and the extent to which and the circumstances under which the premiums may be determined;
- (e) state if that other person is authorised to determine the value of policy benefits, and if authorised, the maximum value of the policy benefits that may be determined under each kind of short-term policy referred to in paragraph (a), and the extent to which and the circumstances under which the benefits may be determined;
- (f) state if that other person is authorised to settle claims under the policies referred to in paragraph (a), and if authorised, the extent to which and the circumstances under which the claims may be settled;
- (g) state the basis on which that other person will be remunerated for services rendered in terms of paragraphs (b) to (f), which basis must be consistent with any requirements, limitations or prohibitions as may be prescribed by regulation;
- (h) oblige that other person to —
 - (i) disclose to policyholders of policies referred to in paragraph (a) -
 - (aa) the name of the relevant short-term insurer or, in the case of Lloyd's underwriters, the term 'certain underwriters at Lloyd's', and the fact that that other person is acting in terms of an agreement contemplated in this section; and
 - (bb) any remuneration payable to that person in terms of an agreement contemplated in this section;
 - (ii) include the name of the short-term insurer or, in the case of Lloyd's underwriters underwriting the short-term policy, the term 'certain underwriters at Lloyd's' in any advertisement, brochure or similar communication which relates to the short-term policy referred to in paragraph (a);

- (iii) keep and maintain proper books of account and other records in respect of the policies referred to in paragraph (a) and allow the short-term insurer or Lloyd's underwriter, its statutory actuary, if appointed, and its auditors full and unfettered access to those books of account and records; and
- (iv) make available to the short-term insurer or Lloyd's underwriter, its statutory actuary, if appointed, and its auditors the policies referred to in paragraph (a) and any information relating thereto, including the names, identity numbers and contact details of policyholders, insured persons and beneficiaries, upon request;
- (i) prohibit that other person to delegate, assign or subcontract any of the functions referred to in paragraphs (b) to (f) to another person;
- (j) state the circumstances under which the agreement will lapse or may be terminated, and the necessary steps that must be taken to ensure the effective and efficient termination of the agreement taking into account the interests of policyholders.

(3) A written agreement referred to in subsection (1), subject to any requirements, limitations or prohibitions as may be prescribed by regulation—

- (a) may not authorise that other person to add an amount to any gross premium referred to in subsection (2)(d);
- (b) may not authorise that other person to deduct any amount from any claims referred to in subsection (2)(f); or
- (c) may provide or prohibit that person to directly or indirectly participate in the profits attributable to the policies referred to in subsection 2(a).

(4) A person that entered into an agreement contemplated in subsection (1) with a short-term insurer or Lloyd's underwriter may—

- (a) render the services contemplated in subsection (1)(a) to (e) in respect of any kind of short-term policy issued by that short-term insurer or Lloyd's underwriter identified in the agreement only in accordance with any requirements, limitations or prohibitions as may be prescribed by regulation; and
- (b) not render any of the services contemplated in subsection (1)(a) to (e) in respect of any kind of short-term policy issued by that short-term insurer or Lloyd's underwriter not identified in the agreement.

(5) Despite any term to the contrary contained in an agreement contemplated in subsection (1), the short-term insurer or Lloyd's underwriter that entered into the agreement remains—

- (a) responsible for compliance with this Act;
- (b) liable for any claims relating to policies included in the agreement, including any claims that may arise because of the failure of that other person to comply with the agreement; and
- (c) the owner of any information and documentation relating to the policies contemplated in the agreement, which must, upon termination of the agreement, be returned to the short-term insurer or Lloyd's underwriter.

(6) Any party to a written agreement referred to in subsection (1) must on request make a copy of that agreement available to the Registrar.

RELEVANT DEFINITIONS

SHORT-TERM INSURANCE ACT NO. 52 OF 1998: SECTION 1

“independent intermediary” means a person, other than a representative, who renders services as intermediary and includes a Lloyd’s correspondent;

“representative” means a natural person employed -

- (a) by or working for a short-term insurer and receiving or entitled to receive remuneration; and
- (b) for the purpose of rendering services as intermediary in relation to short-term policies entered into or to be entered into by the short-term insurer only;

“services as intermediary” means any act performed by a person -

- (a) the result of which is that another person will or does or offers to enter into, vary or renew a short-term policy; or
- (b) with a view to -
 - (i) maintaining, servicing or otherwise dealing with;
 - (ii) collecting or accounting for premiums payable under; or
 - (iii) receiving, submitting or processing claims under,
 a short-term policy;

Financial Advisory and Intermediary Services Act No. 37 of 2002**General Code of Conduct for Authorised Financial Services Providers and Representatives as published in Board Notice No. 80 of 2003**

“associate” -

- (a) in relation to a natural person, means –
 - (i) a person who is recognised in law or the tenets of religion as the spouse, life partner or civil union partner of that person;
 - (ii) a child of that person, including a stepchild, adopted child and a child born out of wedlock;
 - (iii) a parent or stepparent of that person;
 - (iv) a person who is recognised in law or appointed by a Court as the person legally responsible for managing the affairs of or meeting the daily care needs of the first mentioned person;
 - (v) a person who is the spouse, life partner or civil union partner of a person referred to in subparagraphs (ii) to (iv);
 - (vi) a person who is in a commercial partnership with that person;
- (b) in relation to a juristic person -
 - (i) which is a company, means any subsidiary or holding company of that company, any other subsidiary of that holding company and any other company of which that holding company is a subsidiary;

- (ii) which is a close corporation registered under the Close Corporations Act, 1984 (Act No. 69 of 1984), means any member thereof as defined in section 1 of that Act;
 - (iii) which is not a company or a close corporation as referred to in subparagraphs (i) or (ii), means another juristic person which would have been a subsidiary or holding company of the first-mentioned juristic person -
 - (aa) had such first-mentioned juristic person been a company; or
 - (bb) in the case where that other juristic person, too, is not a company, had both the first-mentioned juristic person and that other juristic person been a company;
 - (iv) means any person in accordance with whose directions or instructions the board of directors of or, in the case where such juristic person is not a company, the governing body of such juristic person is accustomed to act;
- (c) in relation to any person -
- (i) means any juristic person of which the board of directors or, in the case where such juristic person is not a company, of which the governing body is accustomed to act in accordance with the directions or instructions of the person first-mentioned in this paragraph;
 - (ii) includes any trust controlled or administered by that person.

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