

Insurance broker fees: Have you adapted your contracts to the requirements set by the Federal Court?

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The case law of the Federal Court concerning retrocession fees («finder's fees»; in German: «Retrozessionen») has startled many actors in the financial markets. With regard to insurance companies and insurance brokers, the question arises as to whether this case law also applies to the payment of broker fees and, if so, what factors must be taken into account in order for broker fees to comply with the relevant legal requirements.

The Federal Court's case law concerning retrocession fees

The Federal Court's case law concerning retrocession fees deals with the remuneration of asset managers (independent asset managers as well as banks). In these cases, the asset managers have already been compensated by the investment customer directly and have often received an additional compensation from a third party (custodian bank). The additional compensation was a commission for bringing in new clients («finder's fee»).

The Federal Court held that the asset manager, being an agent, has an obligation to surrender all direct and indirect benefits that have an inherent connection with the mandate. While the customer may waive the delivery of such benefits, he must first be fully and truthfully informed. In particular, merely remaining silent is insufficient.

Broker fees in the insurance business

As the asset manager, the insurance broker is also assumed to be acting as an agent for the prospective insured and in the insured's interest. However, and contrary to retrocession fees, the customary broker fee paid by the insurer to the broker is a compensation that the insured assumes by paying the premium. From an economic standpoint, the insured pays the broker. The insurer serves only as a «flow heater». With regard to asset managers, the situation is therefore different. As a result, it is questionable whether the Federal Court would consider a broker fee to be a retrocession fee. Only when the broker's remuneration exceeds the customary amount and the broker appropriates additional compensation for himself must one examine whether the case law concerning retrocession fees is applicable and whether the broker has to surrender the received additional compensation. Clearly, additional compensation that is depending on the growth, volume or damage is a retrocession fee.

Requirements for contracts between the parties

Based on the foregoing, the agreements in the business triangle between insured, broker and insurer must meet certain requirements.

The **broker agreement** between the broker and the insured should state that a fee is owed for the broker's activities and that such fee will not be paid directly by the insured but rather indirectly by the insurer out of the insurance premium. The broker should also inform the insured about the amount of the broker fee. Failing to do so, he is owed remuneration in a customary amount. The latter is no retrocession fee.

In the **insurance agreement** between the insurer and the insured, the insurer commits itself to pay the broker fee agreed upon between the insured and the broker.

In the **cooperation agreement** between the broker and the insurer, the insurer must notify the broker that he has settled the broker fee in the agreed amount with the insured. When indirect benefits are involved that have an inherent connection to the mandate, such as additional compensation for bringing in business for the insurer that is depending on the growth, volume or damage, then the broker must, upon demand of the insured, submit a proper accounting and deliver whatever he has so obtained, unless the broker has sufficiently informed the insured about this additional remuneration and the insured has waived delivery of such benefits.

The current FIDLEG draft

The current draft of the Federal Act on Financial Services («FIDLEG») dated June 25, 2014, states that Financial Service Providers may accept benefits only if the customers have waived their claim

for the benefits or if they pass all of the benefits to the customers. A waiver is valid only if the nature and the extent – alternatively the calculation parameters and the range – are disclosed to the customer in advance. Further, services may be deemed independent only when, in connection with providing the service, the Financial Service Providers accept no benefits from third parties or, if benefits are accepted, they are passed along to the customers. Through reference, these provisions shall also apply to insurance brokers.

In our opinion, the same treatment of broker fees and retrocession fees is not justified. Even though a disclosure of the amount of the broker fee in advance is desirable, it must not be forgotten that pursuant to the Swiss Code of Obligations, the agent has the right to a customary remuneration. It is irrelevant whether such remuneration is paid directly by the customer or indirectly through the insurance premium by the insurer.

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