Financial Conduct Authority

FCA
FINANCIAL CONDUCT AUTHORITY

Thematic Review TR14/4

Risks to customers from financial incentives – an update

March 2014

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1. Foreword – by Martin Wheatley CEO

There is no doubt that the way sales staff are paid influences their behaviour - why else would an 'incentive' scheme exist in the first place? Incentives are, by definition, designed to make someone do something: an inducement to act. Incentives are used ideally to reward and incentivise 'good' performance. However, we know this inducement can also have an undesirable effect if poorly designed, with consumers ultimately being worse off. For example, the bonuses earned on payment protection insurance (PPI) sales certainly helped to drive widespread mis-selling. And this is not the only example. We have recently taken action against a number of firms for poor practices within their incentive arrangements.

Eighteen months ago I highlighted this issue and made it clear that, where incentives lead to bad outcomes for consumers, things had to change. We saw numerous examples of poorly designed and administered schemes which created a significant risk of harm to consumers. My message then was 'enough is enough'. As an industry that has had its commitment to its customers questioned, I said firms had to develop a culture that puts their customers first, rather than focusing on maximising profits and bonuses for sales staff.

This was a wake-up call for all areas of the industry. Many firms agreed that the model needed to change and publicly committed to doing so. This was welcomed not only by my organisation but by customers as well. I made a commitment that we would carry out a piece of follow-up work on financial incentives to check how firms had responded to our findings and the guidance which we provided to help them meet our requirements.[1]

That early commitment from firms has brought about changes and it's good to see that significant progress has been made, with a large number of firms changing the way they reward sales staff and advisers to drive better behaviour. We have also seen improvements in the way firms monitor the bad behaviour of staff where they are likely to be influenced by incentive schemes. This is encouraging.

Yet, there is more to do, as this piece of follow-up work highlights, because some firms still need to get better control of their incentive schemes to be confident their staff aren't being induced to deliver the wrong outcome for a customer. It will take time to see if the improvements become part of a genuine cultural change in firms, and whether there are real changes for consumers or whether other pressures put on staff replace sales incentives to similar effect.

This is not something that changes overnight, so we will continue to have a strong interest in this area and it will be part and parcel of our supervisory activities. Firms can't sit back and assume everything is working as it should. They need to build on the progress already made and be vigilant to ensure poor practice does not return.

1 http://www.fca.org.uk/your-fca/documents/finalised-guidance/fsa-fg131

2. Overview

What is this report about?

This report summarises the findings of our follow-up thematic work into financial incentives which assessed whether firms are now managing the risks to consumers.

Who is this report aimed at?

This report is aimed at all firms in retail financial services[2], including smaller firms, with staff who are part of an incentive scheme and deal directly with retail customers, and some small and medium enterprise (SME) customers, where relevant. Trade associations, consumer bodies and consultancy firms may also be interested.

Our findings are relevant to all types and sizes of firms, but where there is information relevant to certain firms this is clearly signposted.

Firms that do not make separate bonus or incentive payments – some of the smallest firms have not understood that they have remuneration arrangements we consider to be a form of incentive scheme, for which our guidance is relevant. For example, where sales staff or self-employed advisers receive all of their remuneration from a proportion of fees, income or commission paid to the firm. We refer to this as '100% variable pay' and explain this further on page 15.

2 We explain which firms are included on page 6 of our guidance 'risks to customers from financial incentives'.

Background – previous work

In September 2012 we published a report on the findings of a thematic review into financial incentives for retail sales staff. This report showed that most firms had incentive schemes that were likely to drive mis-selling, without effective controls in place to manage the risks.[3] Our report highlighted areas of concern and provided draft guidance for firms that was finalised in January 2013. Following the publication of our report, we made it clear that we expected firms to:

- consider if their incentive schemes increased the risk of mis-selling and, if so, how
- review whether their governance and controls were adequate and
- take action to address any inadequacies.

We said we would undertake follow-up work to assess how firms had responded and that we remained open-minded about the need to change or strengthen our rules in this area.

Our latest thematic work

What we did

We have carried out an extensive review of incentives schemes for sales staff across all types of firms. We have also looked at the controls firms are using to mitigate the risk of mis-selling from their incentive schemes. The work included:

- on-site assessment of incentive arrangements at all of the largest retail banks
- an online assessment of incentive schemes at all other firms, apart from the smallest, where we included a sample
- visits to 12 medium-sized firms who took part in the online assessment and
- individual feedback to all the large and medium-sized firms.

What did we find?

Significant change

Our intervention to date has resulted in significant change and we welcome the increased awareness and focus on financial incentives.

All the largest retail banks have either replaced or made significant changes to their incentive schemes to reduce risk to consumers. They have also improved their controls.

Nearly all other firms also appear to have considered our guidance and many have made changes or improvements. The level of engagement and change was less at the smallest firms.

In Section 3 we give examples of changes that have taken place.

More to be done

Although we have seen considerable improvements, we estimate that around one in ten of the firms with sales teams had higher-risk incentive scheme features[4] where it appeared they were not managing the risk properly at the time of our assessment.

3 We set out what we mean by mis-selling on page 9 of our guidance.

Most firms with incentive schemes had at least some improvements to make, for example, in the way they use management information (MI). Almost all of the large and medium-sized firms involved in this work have confirmed to us that they have, or will have, completed improvements by the end of March or shortly thereafter.

In Section 3 we explain, in more detail, the common areas where firms may need to do more to manage incentive risks effectively, in particular:

- checking for spikes or trends in the sales patterns of individuals to identify areas of increased risk
- doing more to monitor poor behaviour in face-to-face sales conversations
- managing the risks in discretionary incentive schemes and balanced scorecards, including the risk that discretion could be misused
- monitoring non-advised sales to ensure staff who are incentivised to sell do not give personal recommendations
- improving oversight of incentives used by appointed representatives
- recognising that remuneration that is effectively 100% variable pay based on sales increases the risk of mis-selling and managing this risk.

Long-term change?

The next 12 months will be important in establishing whether changes to incentive schemes will become part of a genuine change in the remuneration of staff. Firms of all sizes will need to embed their new schemes and controls, and determine if they are delivering the intended outcome and if they will be effective in the long term.

This may be part of a wider programme of cultural change to put the consumer at the heart of their business. We appreciate this will take time.

There is also a question whether new schemes that have eliminated or significantly reduced the amount of bonus driven by sales will last, for example, if there appears to be a negative impact on profits. If firms decide not to maintain such schemes and the risk to consumers increases, controls will need to be strengthened.

To deliver real changes for consumers, firms need to ensure that they do not put pressures on staff to similar effect through other performance management approaches (eg, sales targets) instead of financial incentives. We have said previously that we expect firms to manage the risks from performance management and ensure the risks from incentive schemes are not transferred to other areas. We will carry out work on other performance management approaches.

Smaller firms and sector-specific findings

Generally, our findings apply equally to all sectors and different sizes of firm, although we do highlight some specific points in relation to some of the smallest firms we regulate, which are explained in section 3.

4 In our guidance we gave examples of incentive scheme features that significantly increase the risk of mis-selling, please visit pages 13 to 20 of http://www.fca.org.uk/your-fca/documents/finalised-guidance/fsa-fg131.

Next steps

What we expect firms to do now

We expect all firms, including those that have already been given individual feedback, to:

- consider this publication
- take appropriate action now, including building on what they have already done, to ensure they are managing the risks of mis-selling from financial incentive arrangements and
- read or re-read our guidance, where necessary.

As we have said on page 13 of our guidance, firms may need to take steps to remove features or change incentive schemes if they cannot manage the risk.

What the FCA is doing now

Given the progress made, we are not proposing any changes in our rules at this time but financial incentives will remain on our agenda in 2014.

We will continue to focus on financial incentives through our supervision of firms because it is an important area of inherent risk.

We will take steps to increase the engagement of the smallest firms on this issue, because our work indicates they are less engaged with this work than other firms.

We will also carry out work looking at the related area of how firms manage the performance of their sales staff and whether pressure put on staff (through, for example, sales targets) increases the risk of mis-selling.

The FCA begins supervision of consumer credit firms from 1 April 2014. As this develops, we will be looking at the extent to which financial incentives drive poor customer outcomes as part of our work with these firms.

3.
More detail on key findings

How we assessed firms

Our findings for the largest retail banks are based on in-depth assessments and on-site visits.

Our findings for other large, medium and smaller sized firms are based on firm responses to an online assessment which was carried out between July and October 2013. There were over 400 firms that completed the full assessment, providing information about nearly 800 separate incentive schemes. We also visited 12 of the firms that had completed the online assessment.

Not all firms completed our full assessment. This is because around 40% of firms with sales staff told us they did not have any variable pay that was linked to sales.

We gave individual feedback to the largest and medium-sized firms. We are able to comment on their current position, taking account of how they have responded and the improvement actions they have undertaken or committed to. For the smaller firms, we are only able to comment on their progress at the time of responding to our online assessment last year. Some of these firms may have made further progress in the meantime.

There is more information about incentive arrangements at the largest retail banks in appendix 1. We give more details of the data we gathered through our online assessment in appendix 2.

Significant change to incentive arrangements

We welcome the industry's response to date and the considerable change to reduce risk to consumers across all sizes of firms.

We have seen many firms making changes which include removing particularly risky features and improving controls to reduce the overall risk. There are also improved links between incentive payments and the fair treatment of customers.

Examples of reducing the risk in incentive schemes

One firm changed the way it awarded bonuses by linking them to a balanced scorecard containing a range of measures, including measures solely aimed at rewarding the fair treatment of customers. The scorecard did include an element based on sales results and it was clearly specified how much this would contribute to bonuses. All measures were clearly defined.

The balanced scorecard clearly separated how the bonus was earned:

- 25% – what was sold
- 25% – the results of independent sales quality testing
- 25% – measures like product cancellations and not having any upheld complaints
- 25% – purely customer service measures, eg time taken to call customers back

Another firm introduced a quarterly bonus based solely on measures of customer satisfaction; staff could receive this regardless of their sales results and this amounted to 50% of the incentives available. In addition, bonuses for sales were changed to be paid only once per year and the firm introduced a clearly defined 'gateway' to stop or reduce bonus payments, based on the results of sales quality testing.

Other changes to incentive schemes

In addition to firms removing higher risk features, we have seen:

- fewer short-term bonuses - more quarterly, half yearly or annual payments instead of monthly schemes
- team or branch-based incentives, rather than individual bonuses
- sales quality testing having a bigger impact on incentive payments and/or eligibility for bonuses
- schemes where an element of the bonus is purely driven by customer service measures, eg, as a separate scheme or as part of a balanced scorecard
- caps on the amount of bonus that can be earned.

Large retail banks

The largest banks have either replaced or considerably revised their schemes. At the time of our assessment three banks had completely removed the direct link to sales from some or all of their incentive schemes. The structure and design of incentive schemes appears to be less risky with fewer higher risk features, such as variable salaries and product bias.

Some of the most significant reductions in incentive risks have been in retail banking branches and call centres, for example staff who sell products such as current and packaged accounts. However, some higher risk schemes still remain in other areas of banks, such as investment and protection sales. Many new schemes are discretionary and involve some form of 'balanced scorecard'. Whilst these schemes can reduce the level of risk they can still drive mis-selling. We make comments on this later in this section.

Controls have improved. We have seen stronger governance at the largest firms. They have improved the way they design, approve and manage schemes and senior staff have played a more substantial role.

Controls are better tailored to cover the risks of mis-selling driven by incentive schemes. For example, we have seen improved MI to identify areas of increased risk driven by features of incentive schemes and more pro-active testing of face-to-face sales conversations, using mystery shopping and/or post-sale calls to customers.

At the time of our assessment nearly all large retail banks had at least some improvements to make, most of these have now been dealt with or will be largely completed shortly.

Other large, medium and smaller firms

While there has been progress, there is more of a mixed picture across other firms.

Nearly all the firms that completed our 2013 online assessment had read our guidance. In about one third of incentive schemes that had higher risk features, firms have removed or reduced one or more of these features. Also, in approximately two thirds of incentive schemes firms had either added or improved controls, or were planning to make changes soon.

At the time of completing our assessments, we estimate that around one in ten firms with sales teams had higher risk incentive features (for example, product bias) where it appeared they were not properly managing the risk of incentives causing mis-selling, so improvements were not across the board. Most firms with incentive schemes had at least some improvements to make at the time of our assessment.

Of the largest retail insurance companies, two firms have largely removed the direct link to sales from their incentive schemes.

Almost all of the other large and medium-sized firms involved in this work have confirmed to us that they have, or will have, completed improvements by the end of March or shortly thereafter.

Some firms may have been prompted to take action only because they received our online assessment.

Our online assessment indicated that many firms have made other positive changes to incentive arrangements.

- Firms told us that in three quarters of schemes they had identified the likely mis-selling behaviours that may be driven by their incentive scheme.
- In more than one third of schemes, firms were doing more to stop or reduce bonus payments where sales quality standards were not met. Meaning that over two thirds of all schemes now have this feature. While this is positive, it is important that quality measures are sufficiently material and robust enough to act as a suitable deterrent.
- In schemes where line managers were involved in checking the quality of sales, while also earning incentives based on the sales of their team, nearly all firms had reviewed their schemes for conflicts of interest. Where a conflict had been identified some firms still needed to improve management information and/or carry out credible additional testing to address this conflict.

Smallest firms
Our online assessment covered a sample of the very smallest firms. While we have seen improvements, the responses suggest that the smallest firms are less engaged than other firms. This is explained later in this section. We will seek to engage more with these firms as part of our next steps.

Improving incentive controls

We have seen real improvements in the controls that firms use to manage the risks from their incentive schemes, but there is more to be done and further improvements are still needed in a number of areas previously highlighted in our guidance.

Management information (MI)
Many firms still need to improve the quality of their incentive-related MI. Firms need to make sure they have the right information to identify areas of increased risk from incentive scheme features. MI should help monitor the sales patterns or trends of individual sales staff, which may indicate increased risk. This will also help to target risk-based business quality monitoring and inappropriate behaviour monitoring.

Many schemes had features which might result in spikes or trends in sales (for example, achieving a monthly target which results in an additional bonus) without sufficient MI to identify areas of increased risk.

Example of tailoring MI and controls to incentive scheme features
One firm increased the incentives paid to sales staff if they achieved their target before the end of a quarter. The firm identified the risk that some staff might mis-sell in the run-up to this deadline if they were close to reaching the target, as this would significantly increase their bonus for that quarter.

To manage this risk, the firm used MI to identify any staff who had only just exceeded the target, or just fell short, and looked more closely at their sales patterns and the type of products sold in previous weeks, compared to other times. Any suspicious activity was then subject to additional monitoring to check for mis-selling.

Business quality monitoring
Nearly all firms use some form of routine business quality monitoring as a key element of mitigating the risk of incentives driving mis-selling, but some of the monitoring is not sufficiently risk-based.

Our online assessment showed that some firms did not do any additional monitoring for sales staff who had been identified as being at high risk of mis-selling practices. This might mean, for example, that firms do not have any additional monitoring for staff who sell higher product volumes than others or staff with increased sales in the run up to a bonus threshold. MI should help identify individual sales patterns or trends which may indicate increased risk.

'Inappropriate behaviours'
Routine business quality monitoring is unlikely to be sufficient on its own to effectively monitor for the risk of inappropriate behaviours driven by incentives. By inappropriate behaviour, we mean the way staff might behave during sales conversations, for example, saying something inappropriate because they are motivated by financial gain. We want firms to consider what is actually said during the conversation. Inappropriate behaviour might include not explaining important information, such as the limitations of a product or a customer's eligibility for claims. It could also include pressurising customers to buy a product or giving advice when following a non-advised sales process (see below).

Some firms have introduced or enhanced their approach to using pro-active testing of sales conversations, for example, through mystery shopping or post-sale customer contact. But many firms are not pro-actively checking for these kinds of behaviours. This is a particular issue for face-to-face sales, where we found that firms often did not have adequate checks for inappropriate behaviour. We have seen a reliance on observed interviews to spot these behaviours. However, this approach is unlikely to identify inappropriate behaviours driven by incentives, because staff can alter their conduct accordingly.

Where firms appeared to have pro-active testing in place it often did not check for pressure selling.

While telephone sales are easier to monitor because phone calls can be recorded, firms still need to ensure their approach covers these risks adequately.

In pages 26-27 of our guidance we gave some good and poor practice examples of inappropriate behaviour monitoring. Firms need to satisfy themselves that they are doing enough of this kind

of testing on a risk basis and that this testing is checking for the right behaviours to adequately manage the risks.

Example of introducing more testing for inappropriate behaviours in face-to-face sales

One firm recognised that its monitoring approach of reviewing sales files would not identify inappropriate behaviours like pressure selling or mis-leading customers. Additional testing was introduced using independent staff to contact a sample of customers after they bought a product, using open questions to test what had been said during the sales conversation.

Because the firm's incentive scheme included an accelerator, some of the customer call backs were targeted at the sales of staff where there had been a marked increase in how much they sold after the accelerated rate of reward had kicked in.

Discretionary incentive schemes and balanced scorecards

We have seen an increase in the number of firms using 'discretionary' incentive schemes. When we talk about 'discretionary' schemes we mean schemes where the link between sales and bonus is not completely formulaic and there is an element of discretion in allocating bonuses or subjectivity, for example, in awarding appraisal grades which determine the bonus. Many of the discretionary schemes we have seen are based on a 'balanced scorecard' where staff are appraised against a range of objectives, and not just sales.

While this may reduce risk, it does not eliminate it, as sales are normally still taken into account. We have seen many schemes described as 'balanced' where more than 50% of the bonus came from sales results. Firms should consider if scorecards or objectives are sufficiently balanced.

In addition, discretion could be misused in awarding appraisal grades and bonuses in a way that increases the weight given to sales, which may increase the risk of mis-selling. Sales managers may be biased towards those with better sales results, particularly if they have a conflict of interest in how they are rewarded financially or otherwise themselves, or because they are used to viewing sales results as the most important factor. This might also happen even where a discretionary scheme and individual's objectives do not have any direct link to sales. Firms will need to ensure they can identify when this might occur and take appropriate action.

Firms will still need to have appropriate controls for mis-selling risks in this type of scheme, because sales results can remain a significant factor in determining the level of bonus awarded. Pages 23 and 24 of our guidance states the need to identify spikes and trends in the sales patterns of individual sales staff, for example, in the lead up to the end of a bonus period, to identify areas of increased risk to inform the firm's monitoring. It would not be appropriate to assume that, on its own, the design of a discretionary or balanced scorecard scheme could adequately mitigate the risk of incentives driving mis-selling.

In our work, we saw a number of controls aimed at managing the risk of how discretion is used. These included:

- comparing the sales results of individuals to the bonus they were awarded, across a sales team, to assess the impact on incentive levels
- comparing the outcome of individual appraisals with their bonus payments, to understand how the scheme is working in practice and
- a calibration process to assess the effectiveness and consistency of appraisals.

Example of managing risks in a discretionary scheme
One firm recognised that, although sales staff did not have a specific target to meet, they might sell more in the run up to the cut-off date for the quarter in which their performance would be appraised for bonus purposes. MI was used to identify individual staff with 'spikes' in sales volumes, or unusual trends or sales patterns, and additional monitoring was targeted at the extra sales that occurred at these times.

Monitoring non-advised sales
When firms sell products through a non-advised service and they have incentives linked to how many products are sold, a key risk is that staff will make personal recommendations to influence customer buying decisions.

Some firms providing a non-advised service are not sufficiently monitoring the risk of staff giving advice. This was mainly for face-to-face sales conversations, although some telephone sales areas were also falling short.

Incentives used by appointed representatives
In our guidance (page 6) we explained that, where an appointed representative ("AR") has their own sales staff or advisers, the principal firm remains responsible for managing the risk of mis-selling. Therefore, the principal firm needs to have sufficient understanding of any incentive arrangements in place. This is not always happening.

In 16% of incentive schemes, some or all business was sold through ARs who had their own sales staff. Some of the principal firms informed us they did not have any information, or had only partial information, about the financial incentives schemes the ARs used for their own sales staff or advisers.

While many said they were in the process of getting sufficient information, this suggests that firms with ARs need to do more to understand the risks in the way ARs use incentive schemes.

Smallest firms

In addition to the points in the section 'Improving incentive controls' there are some further points for the smallest firms.

Understanding when remuneration acts like an incentive scheme
Responses to our online assessment suggest that, in instances where staff do not receive a separate bonus or other incentive payment linked to sales, some firms believe they do not have any form of financial incentive scheme. For example, where staff or self-employed advisers receive all of their remuneration from a proportion (fixed or otherwise) of fees, income or commission paid to the firm.

However, we consider remuneration arrangements of this type as incentive schemes for which the guidance is relevant. This is because the level of remuneration an individual can achieve is variable as it is solely based on the products or services taken up by their customers and the fees or income this generates. On page 16 of our guidance we identified 100% variable pay/commission-only arrangements, where no salary is paid, as an incentive scheme feature that significantly increases the risk of mis-selling.

We accept that many smaller firms will have 100% variable pay because of the nature of their business models and we are not directing firms to adopt remuneration approaches that include fixed costs. However, it is important that all firms understand and manage the risks of mis-selling arising from remuneration based on 100% variable pay.

Engagement with guidance
We recognise that the smallest firms may have different business models and the approach they take to managing incentive risks will depend on the nature, scale and complexity of the firms' business (see Section 4 on page 28 of our guidance).

However, our online assessment suggests that the smallest firms with staff subject to incentives may not have acted on our guidance to the same extent as other firms. For example:

- a lower proportion of the smallest firms told us they had been prompted by our guidance to consider their incentive arrangements

- based on their responses, smaller firms were less likely to have sales quality as a factor which impacts on payments made to sales staff or advisers

- the smallest firms were less likely to have any pro-active testing for inappropriate behaviour in face-to-face sales, relying more on measures such as cancellation rates which are dependent on customers identifying any problems themselves.

The smallest firms that have incentive schemes for sales staff or advisers, including 100% variable pay, need to read the guidance carefully, along with this publication, and take action to improve controls where required.

Long-term change?

The next 12 months will be important in establishing whether the changes to incentive schemes will become part of a genuine change in the remuneration of staff. Firms of all sizes will need to embed their new schemes and controls, and determine if they are delivering the intended outcome and will be effective for the long term.

This may be part of a wider programme of culture change to put the consumer at the heart of the business. We appreciate this will take time.

There is a question about whether the many new schemes that have eliminated or significantly reduced the amount of bonus driven by sales will last, for example, if there appears to be a negative impact on profits. If firms decide not to maintain such schemes and the risk to consumers increases, controls will need to be strengthened.

To deliver real changes for consumers, firms need to ensure that they do not put pressures on staff to similar effect through other performance management approaches (for example, through sales targets) instead of financial incentives. We have said previously that we expect firms to manage the risks from performance management and ensure the risks from incentive schemes are not transferred to other areas.

We will carry out work on performance management approaches. We expect firms to be able to demonstrate they have taken appropriate action and are managing these risks. It is important that firms' good work on incentives is not undermined by allowing other pressures on sales staff to prevent the achievement of long-term improvements in consumer outcomes.

4.
Next steps for firms and the FCA

What we expect firms to do now

We expect all firms, including firms that have already been given individual feedback, to:

- consider this publication
- take appropriate action now, including building on what they have already done, to ensure they are managing the risks of mis-selling from financial incentive arrangements and
- read or re-read our guidance, where necessary.

As we have said on page 13 of our guidance, firms may need to take steps to remove features or change incentive schemes if they cannot manage the risk.

What the FCA is doing

We said we were open-minded about considering strengthening our rules depending on how firms responded to our guidance.

We expect firms to continue to make progress with their approach to financial incentives, using the guidance and the findings from this follow-up work. Therefore, given the progress made, we are not proposing any changes to our rules at this time but financial incentives will remain on our agenda in 2014. Financial incentives schemes will continue to be a priority as we begin to consider implementation of MiFID II.

We will continue to focus on financial incentives through our supervision of firms because it is still an important area of inherent risk.

We will take steps to increase engagement on this issue with the smallest firms, because our work indicates they are less engaged with this work than other firms.

We will also carry out work looking at the related area of how firms manage the performance of their sales staff and whether other pressure put on staff (through, for example, sales targets) increases the risk of mis-selling.

The FCA begins supervision of consumer credit firms from 1 April 2014. As this develops, we will be looking at the extent to which financial incentives drive poor customer outcomes as part of our work with these firms.

Appendix 1
Additional data about incentive arrangements at the largest retail banks

This appendix provides more information about incentive arrangements at the largest retail banks.

Appendix 2 provides information about other firms, who completed our online assessment. We do not always hold the same data, or data in exactly the same format, but we have provided information where this is broadly comparable.

1. Incentive schemes

We received information about 44 separate incentive schemes at the largest retail banks, which covered the following product areas:

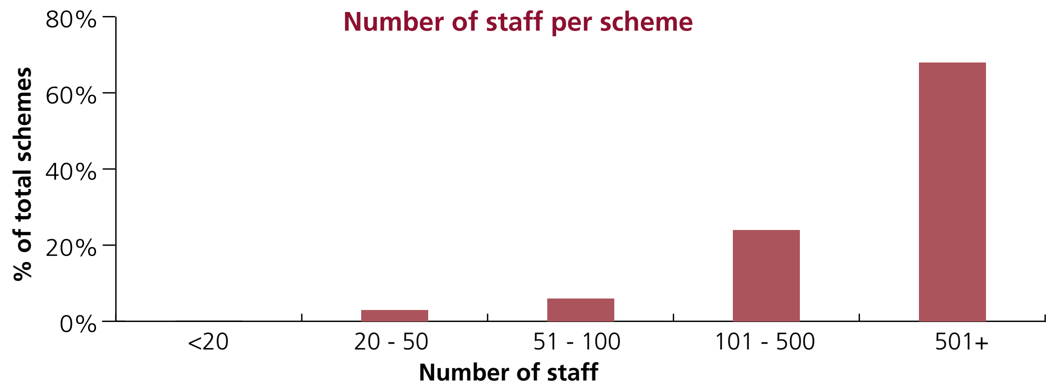
- Current accounts and savings products
- Investments (and related products and services)
- Mortgages
- Life and other protection
- General insurance

In 9 of these schemes there was no direct link between the level of sales and incentive payments. These have been excluded from the information below.

At least one third of schemes have a maximum incentive payment of 20% of salary or more and 10% of schemes have a maximum incentive of 50% of salary or more.

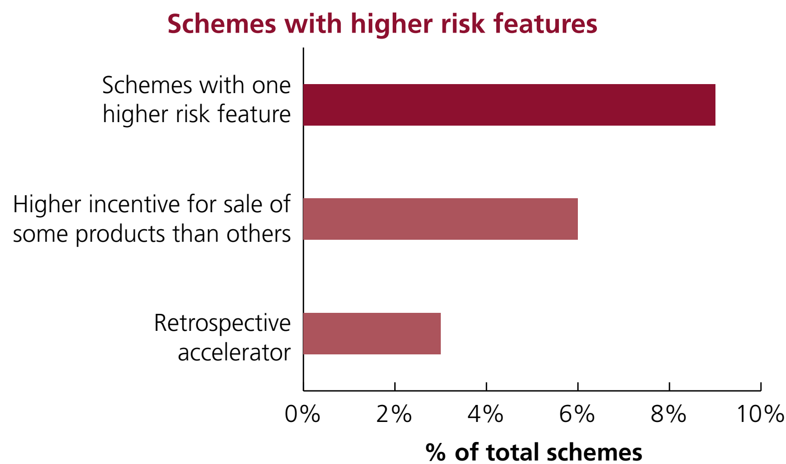
2. Size of sales teams

The vast majority of schemes have over 100 staff.



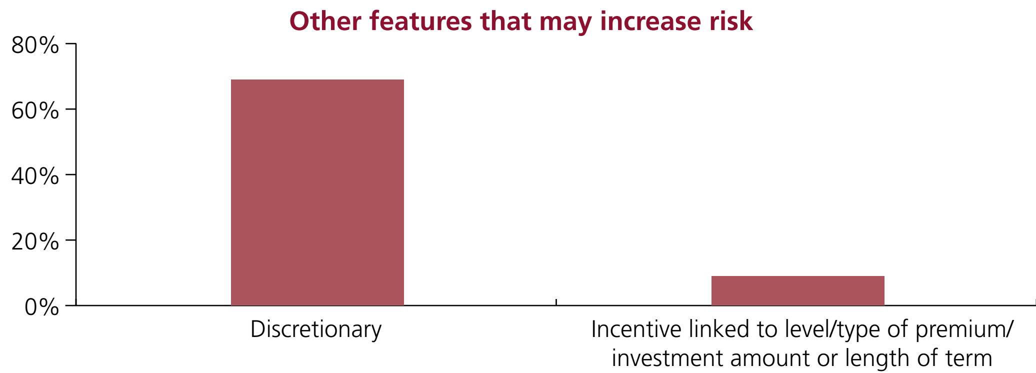
3. Incentive scheme features

In our guidance we gave examples of incentive scheme features that we considered could significantly increase the risk of mis-selling ('higher risk features'). We also gave examples of other incentive scheme features that we considered could increase the risk of mis-selling and features which might reduce the risk. The guidance explains the features in more detail.

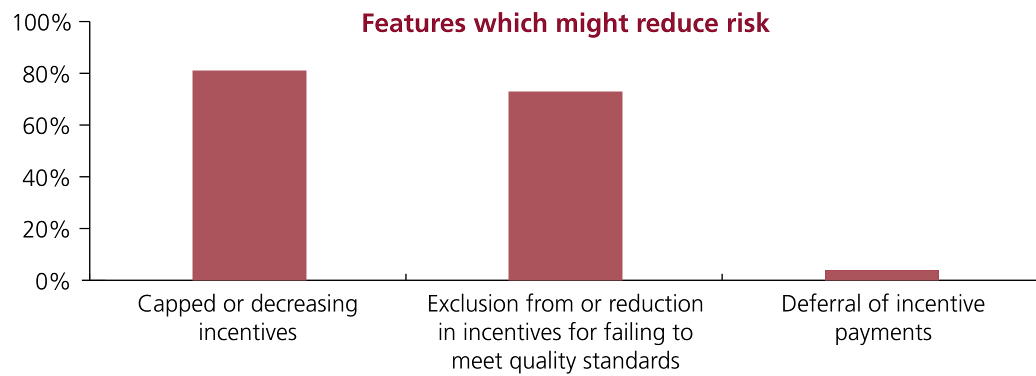


Less than 10% of schemes had a higher risk feature. No schemes have more than one higher risk feature.

Nearly 70% of schemes are discretionary. Discretionary schemes include appraisal or balanced scorecard based schemes (which include a link to sales) where there is an element of discretion or subjectivity in determining bonuses.



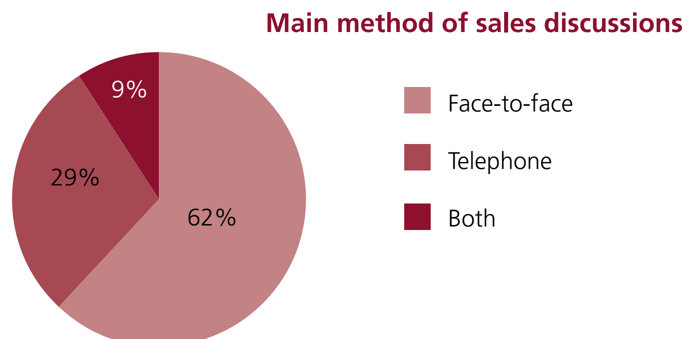
Most schemes exclude or reduce incentives for failing to meet quality standards.



Nearly all schemes reflected results of sales quality testing as a deduction (or exclusion) from bonuses and/or as a separate element of the bonus.

4. Main method of sales discussions

We asked firms whether their sales practices involved conversations with customers by telephone, face-to-face meetings or a combination.



Appendix 2
Additional data about incentive arrangements at other firms

This appendix provides more information, based on our online assessment, about incentive arrangements at firms.

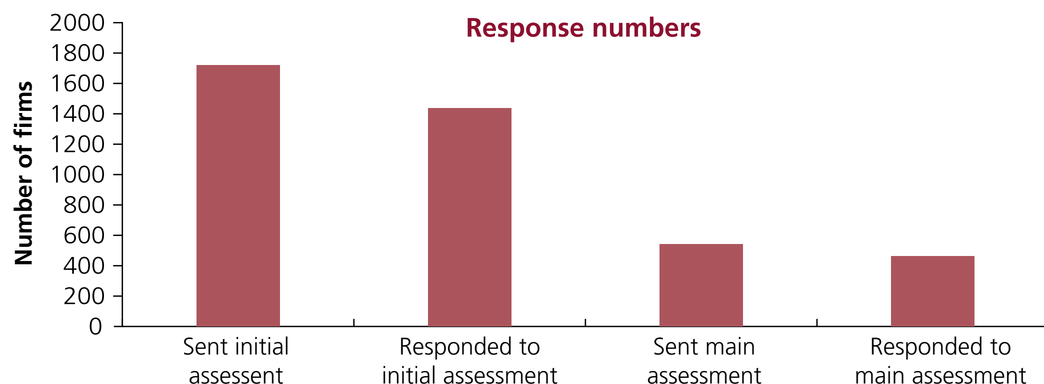
Points to note when looking at this data:

- Some data is set out by size of firm. We refer to large and medium-sized firms, smaller firms and the smallest firms we regulate.[5] The largest retail banks did not complete the online assessment, and are not included in this data, as we assessed them individually.
- The sector analysis contained in this appendix is based on the area of the FCA which supervises each firm, which reflects the most significant business it undertakes.
- We also included in the assessment two large wholesale firms which also have retail sales staff. These are not included where the data is broken down by size of firm, because of the small number of schemes.
- 22 firms told us they had more than 10 incentive schemes. To be proportionate, we asked them to submit the assessment for their 10 largest schemes only. The number of schemes referred to in this appendix and elsewhere in the publication is based only on the number of assessments submitted.

1. Firm response rates

The online assessment was only sent to firms who held permissions relating to retail customers.

An 'initial' assessment was sent to establish which firms had retail sales staff or advisers for which our guidance was relevant, and whether they had variable pay or incentives linked to sales or income generated.



5 This is based on the impact of the firm and the number of retail customers. This relates to the 'C1 – C4' firm categorisations we use in our approach to supervising firms http://www.fca.org.uk/static/fca/documents/factsheet.pdf

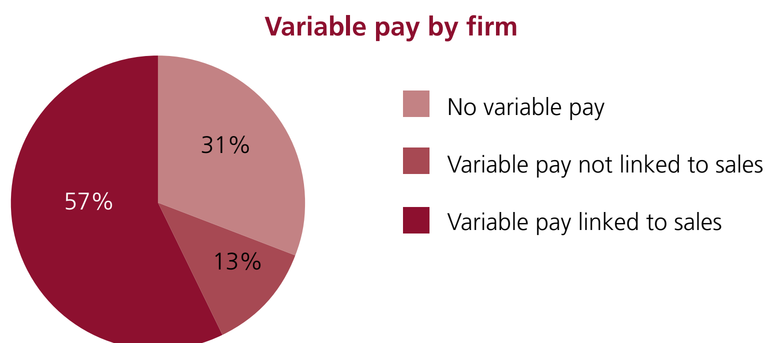
The 'main' assessment was then used to collect information about individual incentive schemes at each relevant firm.

The response rate was 84% for the initial assessment and 85% for the main assessment.

2. Variable pay linked to sales

57% of firms with retail sales staff who responded have variable pay with some link to the level of sales or income generated. 31% had no variable pay, eg, fixed salary only.

Variable pay by firm

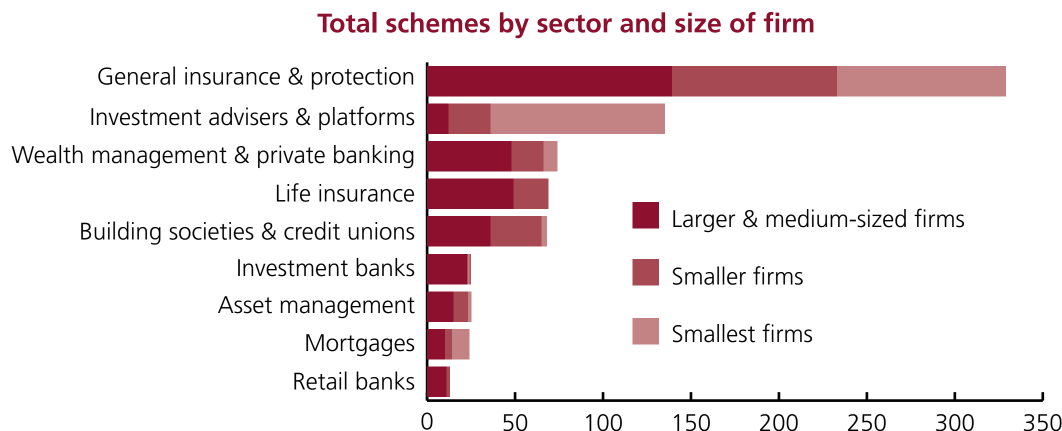


Responses to the initial assessment indicate that 2% of firms with retail sales staff have recently removed the link between the level of sales and variable pay.

3. Incentive schemes split by sector and size of firm

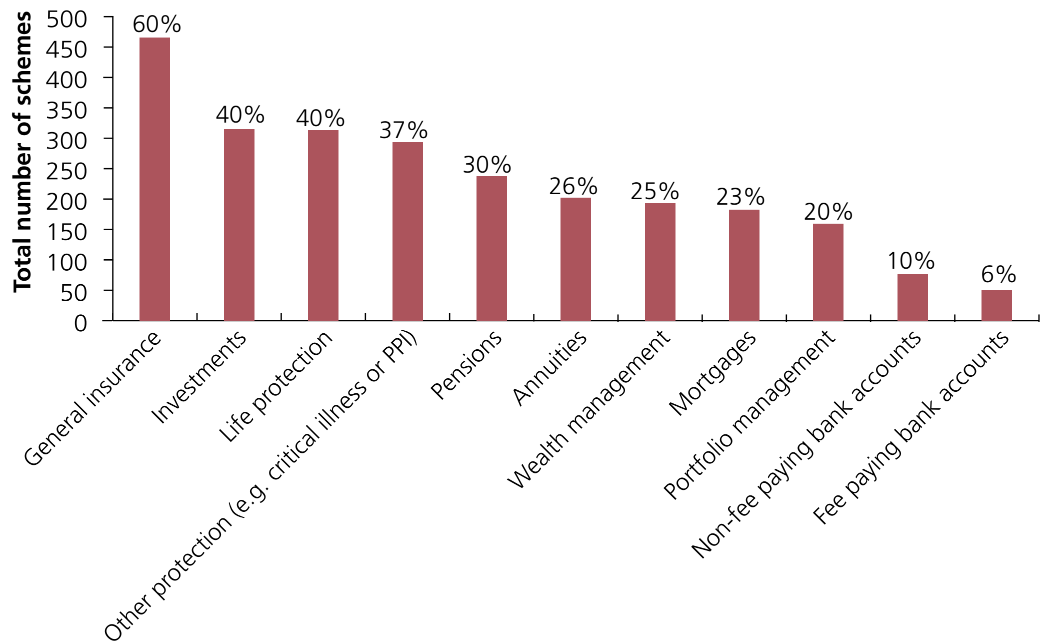
Over 400 firms completed the main online assessment and provided information about nearly 800 separate incentive schemes.

Total schemes by sector and size of firm



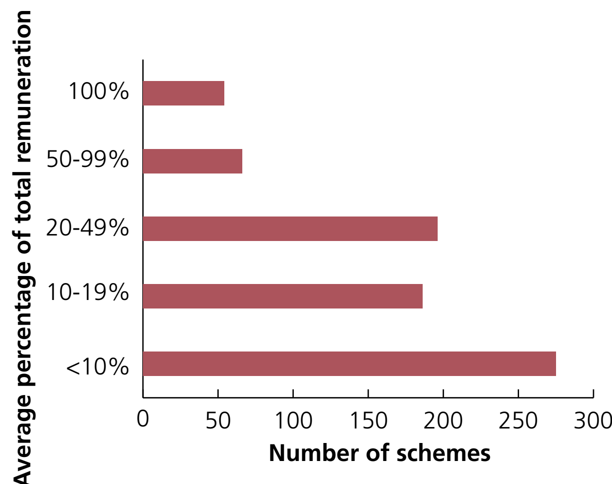
4. Split of products and services linked to incentive schemes

Most incentive schemes involve selling or advising on multiple products or services. General insurance is the most common product offered by sales staff with incentive schemes.



5. Incentive payments compared to total remuneration

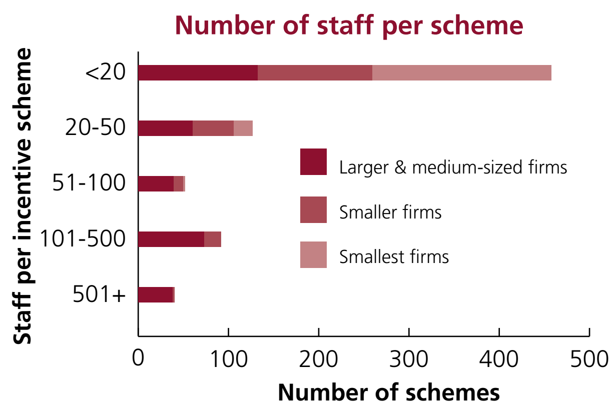
Around half of schemes have average incentive payments of between 10% and 49% of total remuneration.



6. Size of sales teams

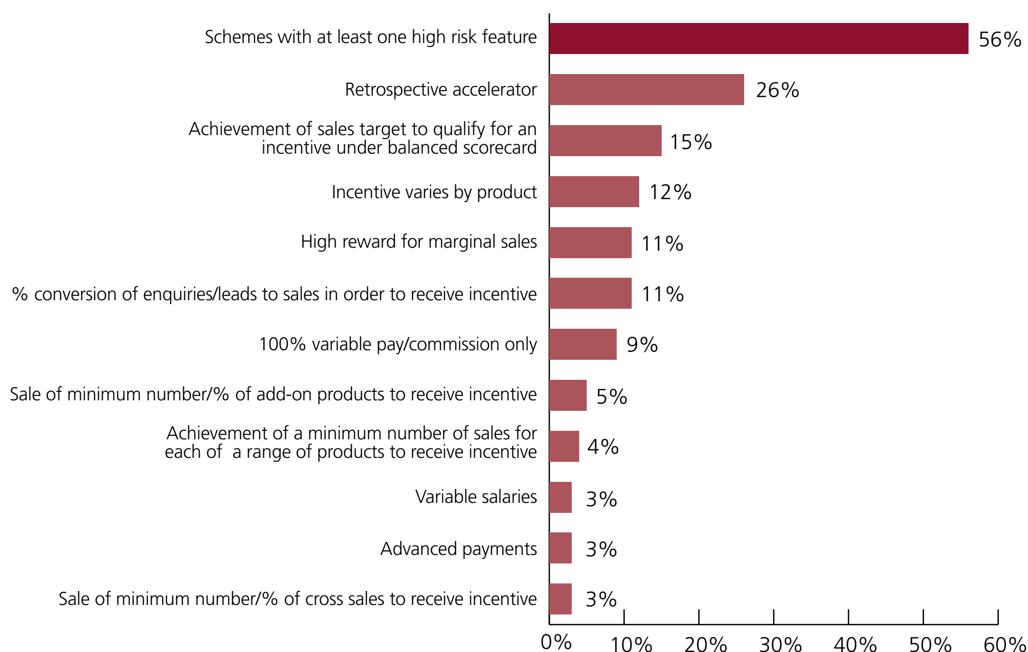
The average number of staff per incentive scheme displays an expected trend between the largest and smallest firms.

A large proportion of schemes have fewer than 20 members.



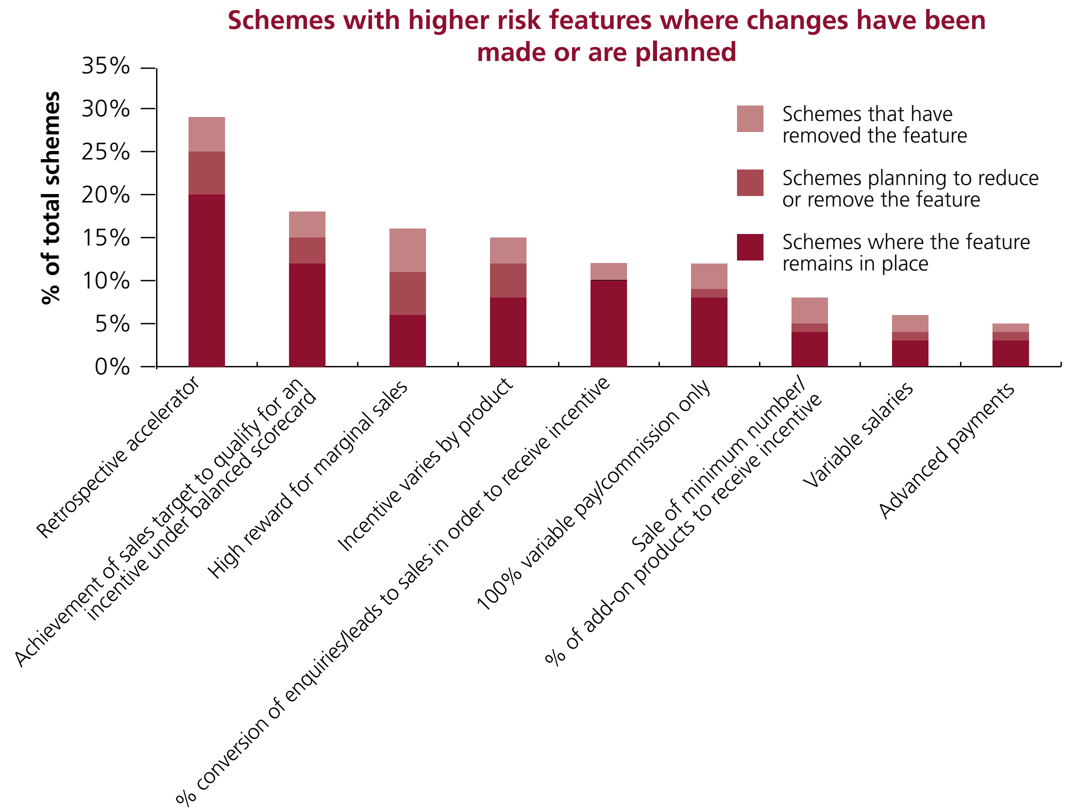
7. Higher risk features in incentive schemes

In our guidance we gave examples of incentive scheme features that we considered could significantly increase the risk of mis-selling ('higher risk features').[6] The guidance explains the features in more detail and the following graphs show the prevalence of these features, at the time of our assessment, and how this has changed since we issued guidance to firms.



6 The features listed are either explained in more detail in our guidance or are self-explanatory.

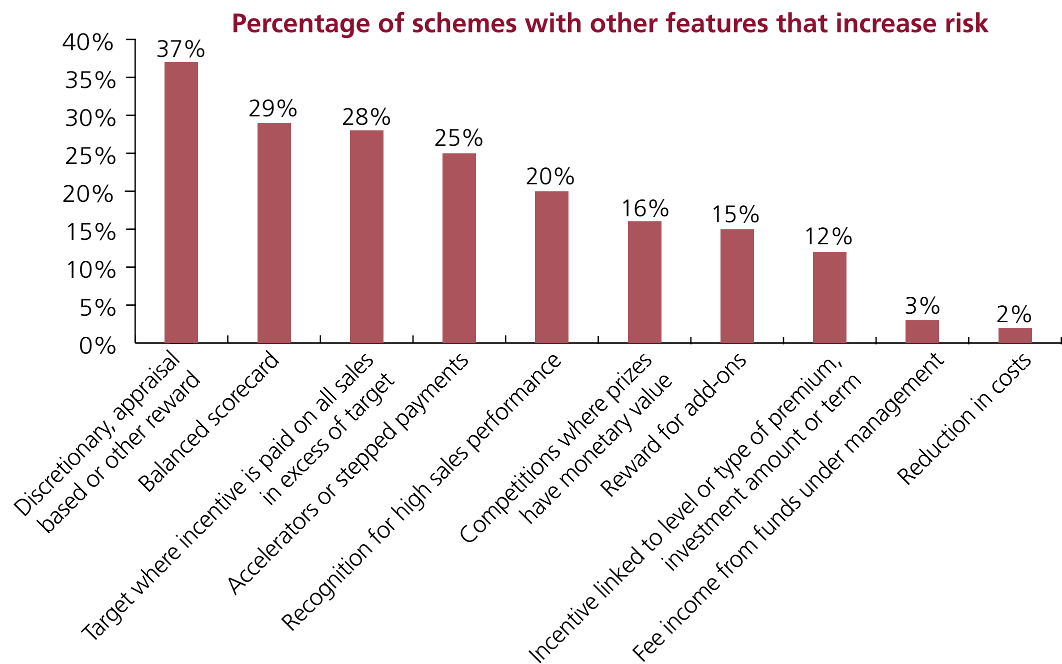
The following graph shows how firms have significantly reduced the use of higher risk features[7] across incentive schemes or are planning to. This is particularly the case for the use of retrospective accelerators, high rewards for marginal sales and incentives varying by product.



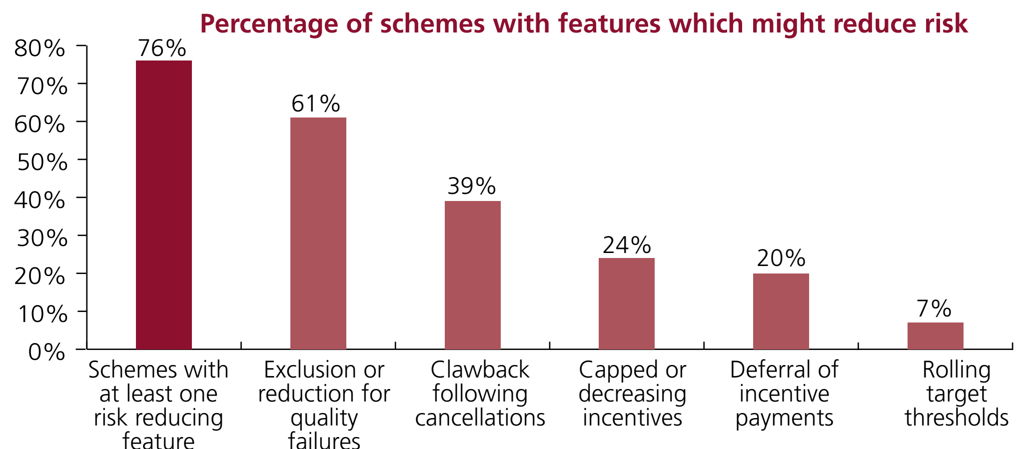
7 This information is provided only for higher risk features where the data is held.

8. Other incentive scheme features

In our guidance we gave examples of other incentive scheme features that we considered could increase the risk of mis-selling and some that might reduce risk. For the purposes of our online assessment we included the feature of 'accelerators or stepped payments' in this set of 'other features', to differentiate it from the higher risk features which can have a bigger impact like retrospective accelerators and high rewards for marginal sales. However, in our guidance we do include accelerators or stepped payments as examples of features that have the potential to increase the risk of mis-selling significantly and firms should continue to assess the risks of such features carefully.

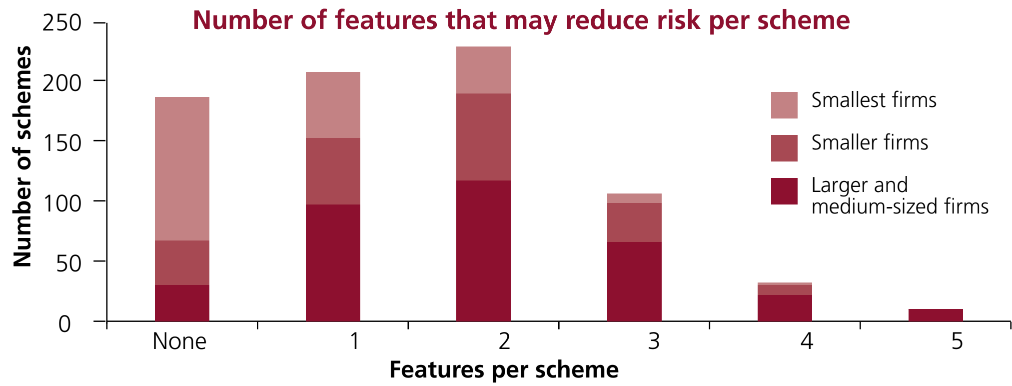


76% of schemes have at least one feature which might reduce the risk of mis-selling, the most common of which is the exclusion or reduction of bonus from a link to sales quality testing.



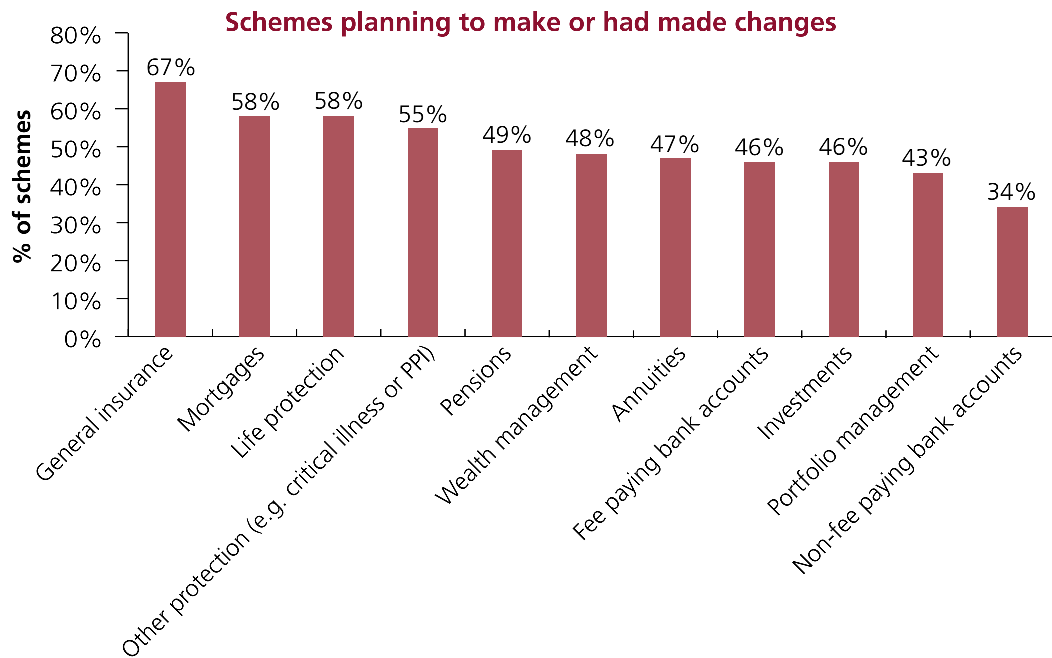
9. Frequency of features that may reduce risk

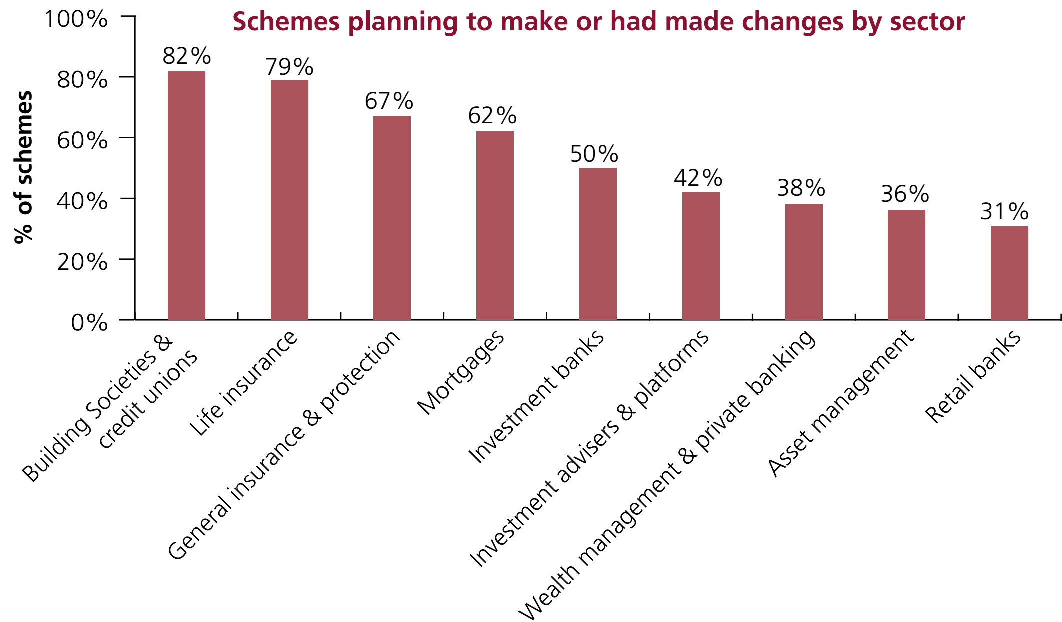
Most schemes have one or more features that may reduce risk.



10. Changes to incentive schemes by product or service

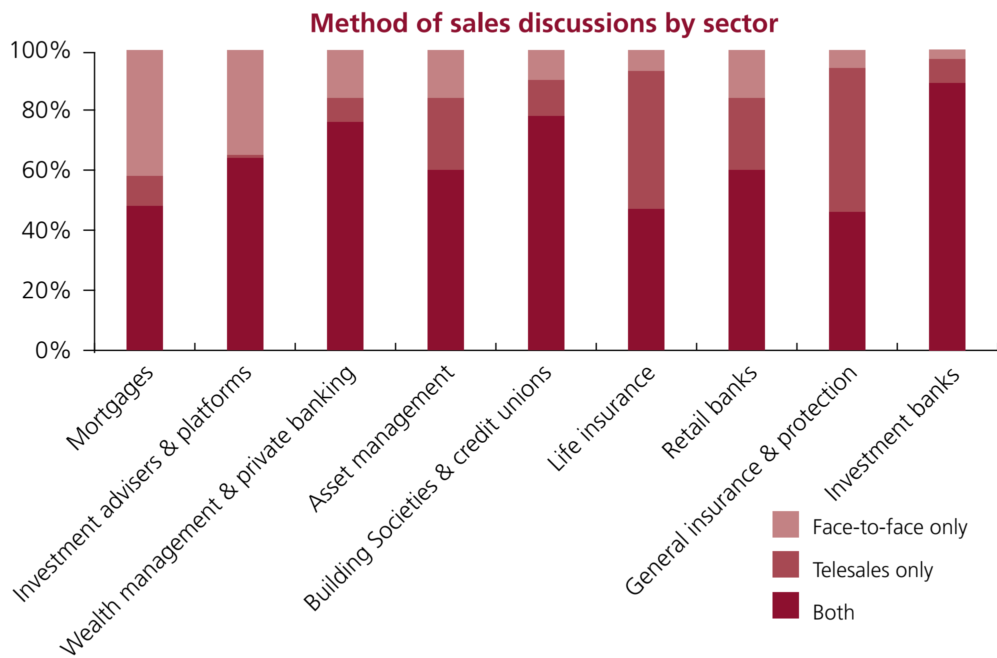
For each of their schemes, firms told us if they had made, or were planning to make, changes to their incentive scheme and/or controls after being prompted by our guidance. This is set out in two graphs by products/services and then by sector. Most incentive schemes involve selling or advising on multiple products or services.





11. Method of sales discussions

We asked firms whether their sales practices involved conversations with customers by telephone, face-to-face meetings or a combination.



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