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INSURERS

Managing the most significant
emerging regulatory risks in 2021

Building
RESILIENCE

Today's speakers



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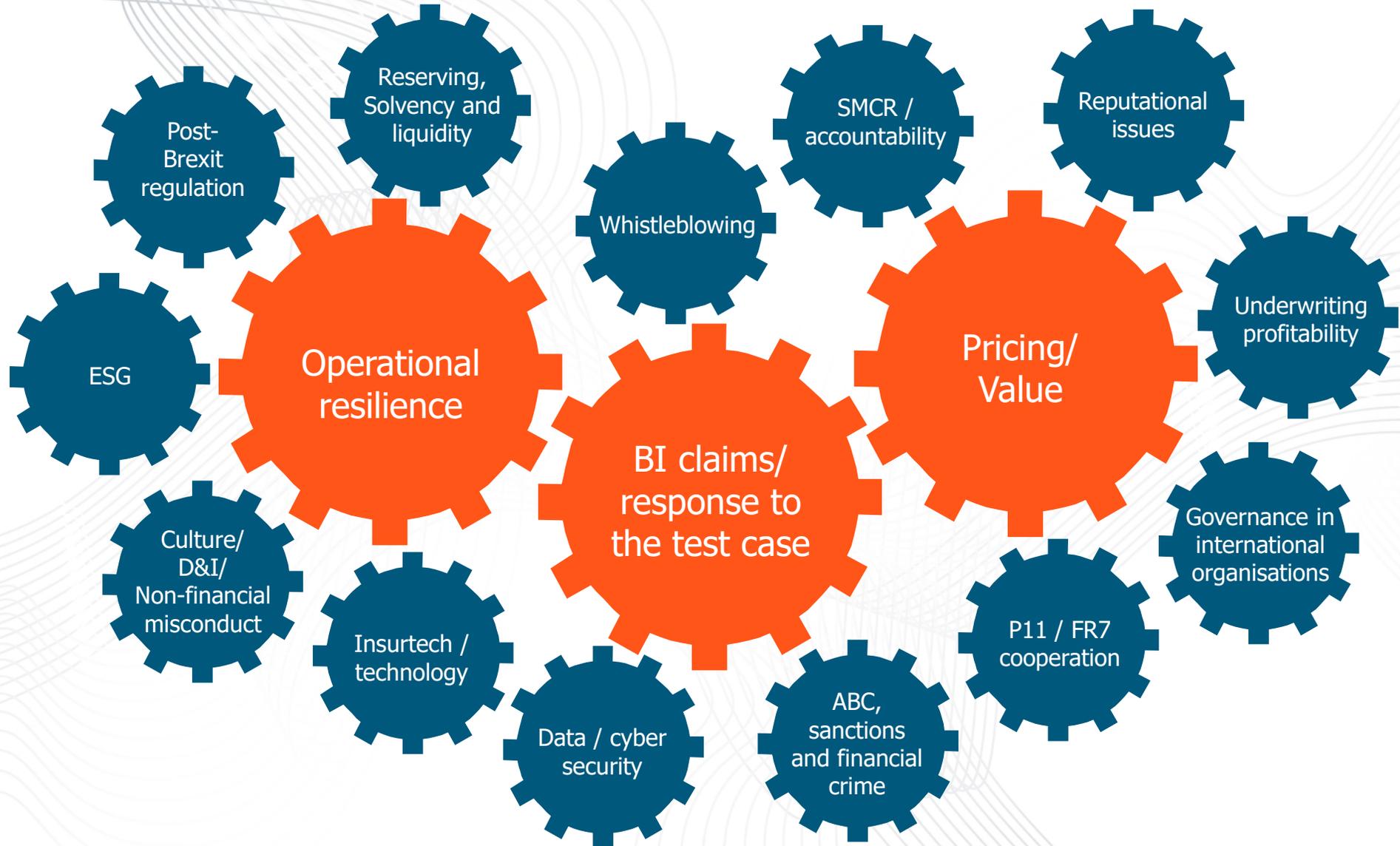


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Overview



Regulatory risks from Covid-19 business interruption claims

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Handling BI claims

- ▶ Relevant regulatory rules
- ▶ FCA “expectations” / soft rules
- ▶ Key areas of focus
- ▶ Regulatory risk for firms

Rules relevant to claims-handling (1)

- ▶ *A firm must pay due regard to:*
 - *the interests of its [policyholders] and treat them fairly*
 - *the information needs of its [policyholders], and communicate information to them in a way which is clear, fair and not misleading*

Principles 6 and 7

Rules relevant to claims-handling (2)

- ▶ *A firm must act honestly, fairly and professionally in accordance with the best interests of its customer*

ICOBs 2.5-1 (IDD)

Rules relevant to claims-handling (3)

- ▶ *An insurer must:*
 - (1) *handle claims promptly and fairly*
 - (2) *provide reasonable guidance to help a policyholder make a claim and appropriate information on its progress*
 - (3) *not unreasonably reject a claim (including by terminating or avoiding a policy); and*
 - (4) *settle claims promptly once settlement terms are agreed*

ICOBS 8.1

FCA “expectations” / soft rules

- ▶ 19 March 2020: FCA webpage – our expectations of general insurance firms
- ▶ 15 April 2020: ‘Dear CEO’ letter on insuring SMEs: Business Interruption
- ▶ 17 June 2020: Guidance for firms on handling BI claims
- ▶ 3 August 2020: Statement on deductions to account for government support
- ▶ 18 September 2020: Post-High Court ‘Dear CEO’ letter
- ▶ 22 January 2021: Post-Supreme Court ‘Dear CEO’ letter
- ▶ Finalised guidance expected shortly on evidence necessary for proving the presence of Covid-19

Nine key areas of focus

- ▶ Board & SMF engagement
- ▶ Communications
- ▶ Reassessments of claims and complaints decisions
- ▶ Reopening settlements
- ▶ Stopping the clock
- ▶ Ability to take account of government support
- ▶ Evidence to substantiate claim
- ▶ Who bears legal costs of further litigation
- ▶ Naming and shaming

Regulatory risk for firms

- ▶ FCA review of Covid-19 claims-handling likely to lead to Enforcement referrals:
 - Firms with unduly slow or unfair claims-handling
 - Insufficient or misleading communications
 - Inadequate reassessments in light of Supreme Court
 - Failure to pay claims promptly once agreed
- ▶ 'Breaches' of soft rules
 - Quasi-punitive actions by FCA supervisors

Operational resilience

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Operational resilience - overview

- ▶ Operational resilience is the ability of firms and the financial sector as a whole to prevent, adapt, respond to, recover and learn from operational disruptions
- ▶ Operational disruptions can have many causes including, for example, technology failures when making changes to systems. Some disruptions may also be caused by matters outside of a firm's control, such as a cyber-attack or wider telecommunications/power failure
- ▶ A suite of PRA and FCA co-ordinated proposals was released for consultation on 5 December 2019. These contain new requirements to strengthen operational resilience in the financial services sector
 - **The PRA, FCA and BoE shared policy summary** - Building operational resilience: impact tolerances for important business services
 - **PRA Consultation Paper** - Building operational resilience: impact tolerances for important business services (CP29/19) – includes a draft Supervisory Statement
 - **FCA Consultation Paper** - Building operational resilience: impact tolerances for important business services (CP19/32) – includes a chapter on outsourcing
 - **PRA Consultation Paper: Outsourcing and third party risk management** (CP30/19) – includes a draft Supervisory Statement
- ▶ The consultation closed on 1 October 2020. The final rules to be released shortly and firms will be expected to comply by the end of 2021

Recap on existing regulatory framework

- ▶ **PRA Fundamental Rule 5** - *A firm must have effective risk strategies and risk management systems.*
- ▶ **PRA Fundamental Rule 6** - *A firm must organise and control its affairs responsibly and effectively.*
- ▶ **FCA Principle for Businesses 3** - *A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.*
- ▶ **FCA Handbook**
 - SYSC 3.1.1R and SYSC 3.2.6R deal with the establishment and maintenance of systems and controls, in relation to the management of operational risk
 - SYSC 13 includes rules and guidance in relation to 'Operational risk systems and controls for insurers' (including outsourcing)
- ▶ **PRA Rulebook**
 - Requirement that firms' boards should approve, regularly review and implement a written **outsourcing policy** (Conditions Governing Business 2.4(1))
 - Requirement for **business continuity plans** (Conditions Governing Business 2.6)
 - SMF 24 Chief Operations Function and prescribed responsibility (in relation to outsourcing)

Lessons learned from previous enforcement actions

- ▶ Enforcement focus has generally been on IT outages and cyber attacks
- ▶ Risks associated with change management projects
- ▶ The importance of oversight of critical outsourced services
- ▶ Firms may not be able to avoid disruptive events; however, you must have plans in place to respond to them if they do occur
- ▶ Escalation procedures when an incident occurs are critical

The new proposals – objectives

(1) Prioritising the things that matter

Boards and senior management should prioritise those activities that, if disrupted, would pose a risk to the stability of the UK financial sector (financial stability) or the firm's safety and soundness

(2) Setting clear standards for operational resilience

Firms should articulate specific maximum levels of disruption, including time limits within which they will be able to resume the delivery of important business services following severe but plausible disruptions (setting impact tolerances)

(3) Investing to build resilience

Firms should have contingency arrangements in place to enable them to resume the delivery of important business services, taking action in advance to ensure that firms' important business services are able to remain within impact tolerances in severe but plausible scenarios

What will the new regime look like in practice?

- ▶ Identifying important business services
- ▶ Setting impact tolerances
- ▶ Mapping
- ▶ Scenario testing
- ▶ Governance
- ▶ Conducting lessons learned exercises
- ▶ Communication plans
- ▶ Creating a self assessment document

Renewed focus on outsourcing

- ▶ The PRA CP intended to “modernise” the framework for outsourcing and third party management. It includes a new draft supervisory statement.
- ▶ The FCA is not proposing changes to the FCA’s Handbook rules and guidance on outsourcing or third-party service provision as part of its consultation. However, outsourcing is flagged by the FCA as key to effective ‘mapping’ of important business services.
- ▶ **Key considerations**
 - Board engagement on outsourcing
 - Outsourcing policy
 - Pre-outsourcing phase
 - Outsourcing agreements
 - Intragroup outsourcing and branch “outsourcing” to head office

2021 – The year of ‘value for money’ regulation in insurance?

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Why now?

FSA (2001 – 2012) – “We are not a price regulator”

PPI – More than mis-selling?

2015 - FCA obtains concurrent competition powers

Big data

IDD

How the FCA will regulate for 'value for money' in 2021?

1

Publication of value measures more broadly

2

Product governance (including distribution chain governance)

3

Specific new conduct rules designed to prevent identified unfair pricing practices

4

Ad hoc measures (e.g. 2020 FCA requirement to perform 'Covid value for money assessments')

Publication of value measures

“the sunlight
remedy”



Value measures – metrics to be reported (SUP 16.27.11R from 1 July 2021)

(1) number of policy sales;

(2) total gross retail premiums (written);

(3) number of claims registered;

(4) average number of policies in force;

(5) claims frequency;

(6) number of claims accepted;

(7) number of claims rejected;

(8) claims acceptance rate;

(9) total claims pay-out cost;

(10) average claims pay-out;

(11) amount that the top 2% of claim pay-outs are above;

(12) names of the five largest distribution arrangements;

(13) number of claims walkaways;

(14) number of claims complaints; and

(15) claims complaints as a percentage of claims.

What will the FCA publish?

SUP
16.27.19G

- Claims frequency
- Claims acceptance rate
- Average claims pay-out
- Claims complaints as a percentage of claims

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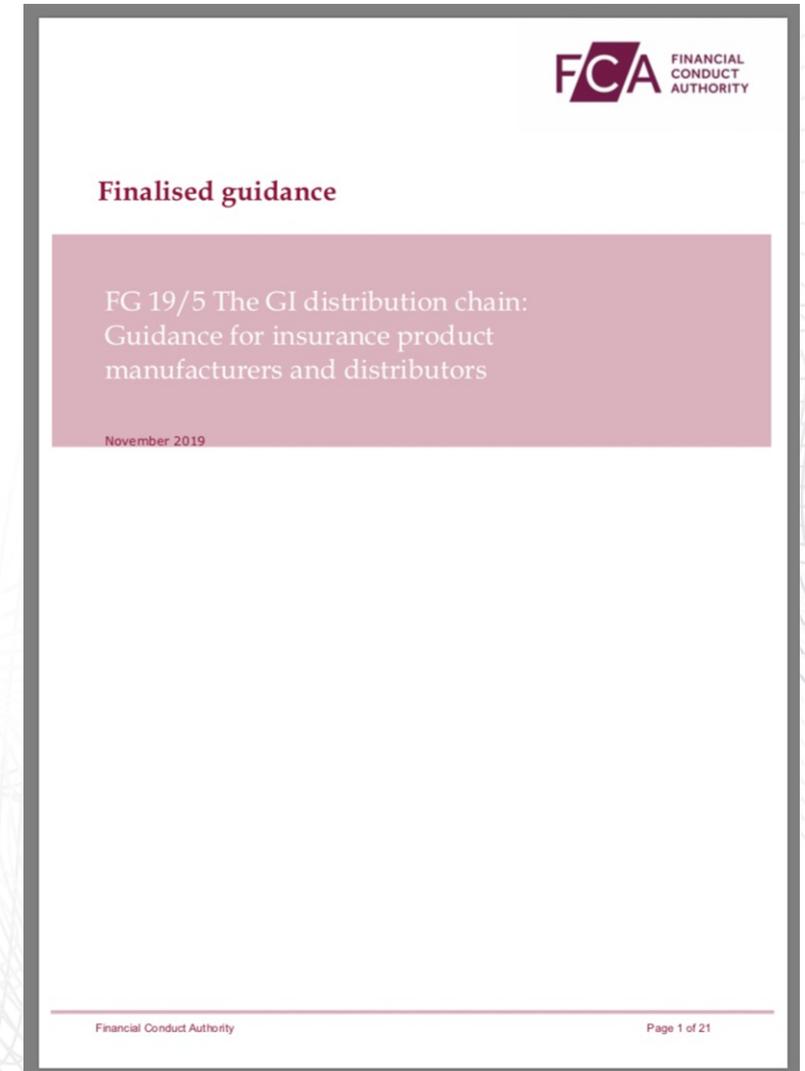
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November 2019 FCA guidance following thematic review work

- ▶ FG19/5 – “The GI distribution chain: Guidance for insurance product manufacturers and distributors”
- ▶ Focussed on ensuring customer value via:
 - Product design process
 - Product distribution strategy
 - Product review process



CP 20/19



General insurance pricing practices market study Consultation on Handbook changes

Consultation Paper
CP20/19***

September 2020
(Updated December 2020)

Proposed new PROD 4.2.14E R

– Defining ‘value’

In PROD 4 ‘value’ means the relationship between the overall price to the customer and the quality of the product(s) and/or services provided.

The assessment of value must include consideration of at least the following:

- (1) the nature of the product including the benefits that will be provided, their quality, and any limitations (for example in the scope of cover, exclusions, excesses or other features);
- (2) the type and quality of services provided to customers;
- (3) the expected total price to be paid by the customer when buying or renewing the insurance product, and the elements that make up the total price. This will need to include consideration of at least the following:
 - (a) the pricing model used to calculate the risk premium:
 - (i) for the initial policy term; and
 - (ii) any future renewal;
 - (b) the overall cost to the firm of the insurance product (including the underwriting and operating of the product) and, where relevant, any other components of a package;
 - (c) the individual elements of the expected total price to be paid by the customer including, but not limited to the price paid for: (i) the insurance product including any additional features which are part of the same non-investment insurance contract for example add-ons or optional cover; (ii) any additional products, including retail premium finance, offered alongside the insurance product; (iii) the distribution arrangements, including the remuneration of any relevant person in the distribution arrangements, and including where the final decision on setting the price is taken by another person);
- (4) how the intended distribution arrangements support, and will not adversely affect, the intended value of the product.

Proposed new evidential provisions - 4.2.14JE

- (1) A non-investment insurance product will not be providing fair value where:
 - (a) the difference between the risk price to the firm and the total price paid by the customer bears **no reasonable relationship** to:
 - (i) the actual costs incurred by the firm or any another person involved in the distribution arrangements;
 - (ii) the quality of any benefits (including of the insurance product or any additional products); or
 - (iii) the costs or quality of any services provided in connection with the insurance product or additional products, by the manufacturer or any another person involved in the distribution arrangements;

Proposed new PROD 4.2.14M R - information to be obtained from distributors

A firm must obtain from any person in the distribution arrangements all necessary and relevant information to enable it to assess the remuneration associated with the distribution arrangements to allow it to assess the ongoing value of the product, including at least:

- (1) the total costs of the distribution arrangement whether as part of the premium or not, including in relation to additional products;
- (2) a sufficiently detailed breakdown of the costs in (1) identifying the type and level of remuneration of each person in the distribution arrangements together with an explanation of the services provided by that person; and
- (3) confirmation from any firm in the distribution arrangements that any remuneration is consistent with their regulatory obligations including SYSC 19F.2.

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CP20/19 – Proposed ban on ‘price walking’

Proposed new
rules for
ICOBS 6B
(home and
motor
insurance
renewals)

- 6B.2.1R A firm must not set a renewal price that is higher than the equivalent new business price
- Can take into account any additional risk information it has acquired during the policy term, where this is information the customer would be asked to disclose if they were a new business customer

Proposed 'no price walking' SMF attestation

ICOBS 6B.2.26R

A firm must make and retain written records of how it continues to satisfy itself that it does not systematically discriminate against customers based on tenure

ICOBS 6B.2.31R

An appropriate senior manager of a firm must provide an attestation that the firm:

- Is and has been complying with the rules in this chapter throughout the reporting period; and
- Is satisfied that the pricing of its home insurance and motor insurance renewal business and related sales practices are consistent with the objectives of the rules as set out in ICOBS 6B.1.3G and does not discriminate against customers of longer tenure

PS: Proposed new rules re: auto-renewals

- ▶ FCA wishes to make it easier for customers who wish to cancel the auto-renew feature
- ▶ Proposed new rules at ICOBs 6A require firms to provide *“a range of different easy and accessible methods for cancelling the automatic renewal feature in the customer’s contract”*
 - Must include telephone, post and email/online
 - Cancellation must be free of charge and available at any time

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This document provides a general summary only and is not intended to be comprehensive. Specific legal advice should always be sought in relation to the particular facts of a given situation

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