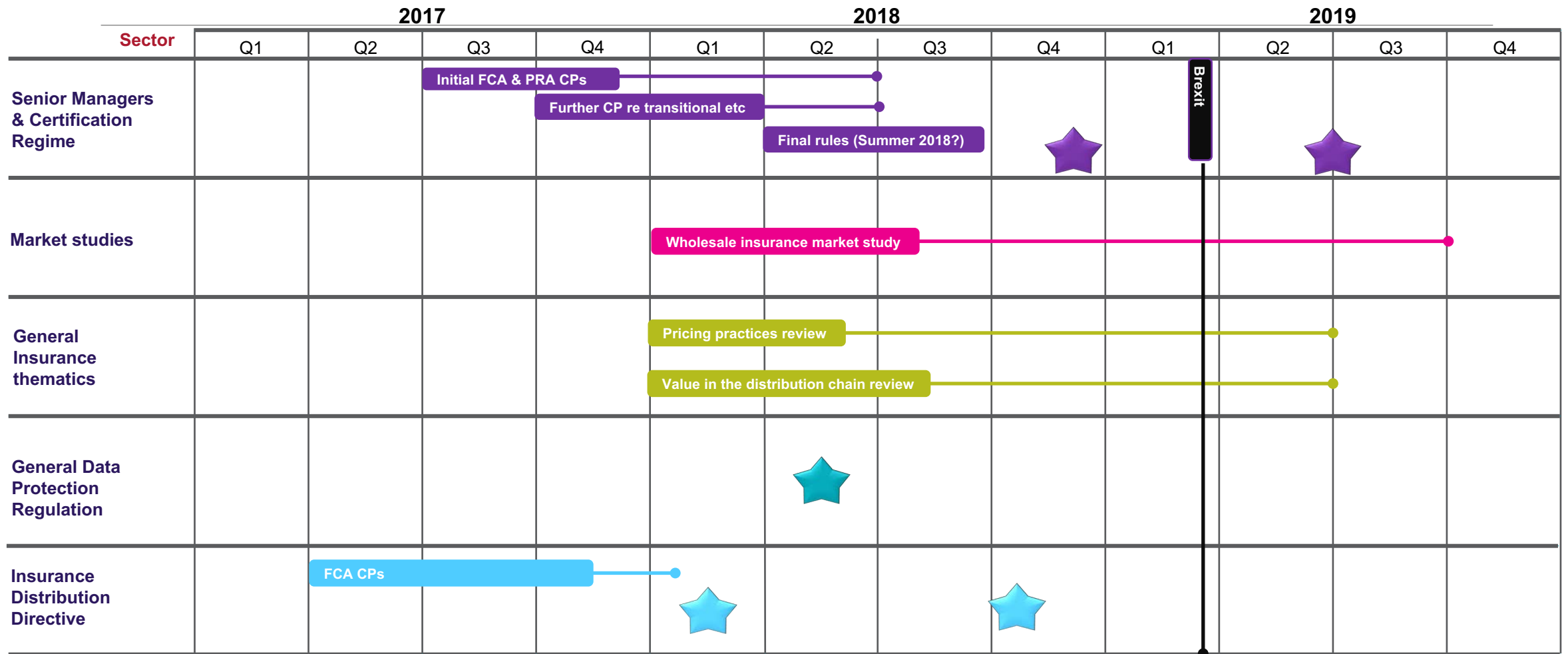




INED FORUM_FEBRUARY 2018

2017 – 2019: Key Dates for the insurance sector



Insurance Distribution Directive (IDD)

Background and Purpose

- The IDD replaces its predecessor - the Insurance Mediation Directive
- IDD must be transposed by 23 February 2018
 - *(note: European Commission confirmed on 20/12/17 that the application date of the IDD will be postponed until 1 October 2018, although Member States would still be required to transpose the IDD into national legislation by 23 February 2018).*
- Applies across the EEA area notwithstanding Brexit looming
- Purpose of IDD is to:
 - Ensure level playing field throughout the EEA
 - Ensure level playing field for all participants in the distribution of insurance
 - Strengthen customer protection

Key changes

- **Conduct of Business for non-investment insurance business**

- **Wider applicability**

- **Large risks for commercial customers** - Additional requirements will apply to firms distributing large risks for “commercial customers” where the risk is located within the EEA (distribution of risks for “retail customers” are already included)
 - **Wholesale intermediaries and other intermediaries not in contact with the end customer** - Additional requirements will apply to ALL intermediaries carrying out insurance distribution business regardless of whether they are in direct contact with the end customer. EG, wholesale intermediaries and Lloyds brokers will be subject to obligations including the new “customer’s best interests rule” and an associated prohibition on remuneration and performance management practices which would conflict with the Customer’s Best Interest rule.

- **General Principles and Customer’s Best interests**

- A set of general principles applicable to all insurance distributors will be introduced. These are overarching requirements, which apply in a similar way to the FCA’s Principles for Businesses, and will include a new “Customer’s Best Interests” rule.

- **Disclosure**

- Remuneration: Firms will need to comply with additional requirements in relation to the disclosure of remuneration
 - Product: Additional information to be disclosed including a new obligation to provide an Insurance Product Information Document (IPID)

- **Selling practices**

- Customers must consent/agree to receiving documents by website/non-paper medium
 - Additional provisions in respect of a customer’s demands and needs will be introduced as well as new requirements in respect of cross-selling activity

Key changes

- **Minimum necessary knowledge**

- All employees (including management) involved in insurance distribution must have appropriate knowledge and ability (by meeting the “minimum necessary knowledge” criteria) and be able to demonstrate a minimum of 15 hours in continuing professional development every year.

- **Product Oversight and Governance**

- Specific requirements are set out in the Product Oversight and Governance Regulation (POG Regulation) in respect of the manufacture (and distribution) of products and it will be key for firms to ensure they understand their associated responsibilities as either a manufacturer or distributor (or both). Firms will need to ensure they have systems and controls in place for the design, approval, marketing and ongoing management of products throughout their lifecycle.

- **Ancillary Insurance Intermediaries (AIs)**

- A new category of intermediary will be introduced, divided into three sub sets: “In-scope AIs”; “Connected Travel Insurance (CTI) providers”; and “Out of scope AIs.”
- Additional requirements are placed on those firms distributing products through the out of scope AIs including the requirement to ensure there are appropriate and proportionate systems and controls in place to comply with the “IDD minimum requirements” including the Customer’s Best Interests rule.

- **Passporting Regime**

- Various changes will be made to the passporting regime (whilst firms are still able to passport) in particular a more detailed process is to be followed than was the case under the IMD, and a new notification regime will apply to firms passporting for the first time.

Changes for Reinsurance

- CASS 5 to be mandatory for reinsurance mediation
- Use only authorised or exempt insurance intermediaries for insurance distribution
- Complaints procedures to cover commercial customers, including reinsurance transactions
- Minimum 15 hours CPD for anyone involved in reinsurance distribution activities

Key tasks



What YOU should be asking?

- Who is co-ordinating the IDD project?
- Have you got an Action plan? What are the key workstreams – Wordings for IPID; Professional Development?
- Are you on track?
- How are you communicating with your coverholders?
- How are you engaging with Legal/Compliance Representatives from EU jurisdictions to consider local implementation?
- Who is updating the firms policies and procedures around Product Governance, Training & Competence, Conflicts of Interest?
- How are you going to train ALL employees on the NEW requirements?

Senior Managers and Certification Regime (SMCR)

What next?

- Extension of the bank/insurer regime to all FCA-regulated firms which was implemented following Parliamentary recommendation to develop a new accountability system
- Three consultation papers have been issued
- The new rules will start when the Treasury sets the dates (assumed late 2018 for insurers and mid – late 2019 for solo regulated firms)
- FCA aims to ensure the regime is proportionate

The changes

Three categories of firm

1. **Enhanced Firm**– small proportion of solo-regulated firms that will have to apply extra rules (eg firms with total intermediary regulated business revenue of £35m or more p.a.)
2. **Core Firm** – Most of you are likely to be a core firm
3. **Limited scope firm** - some firms will have a reduced set of requirements

The new structure...

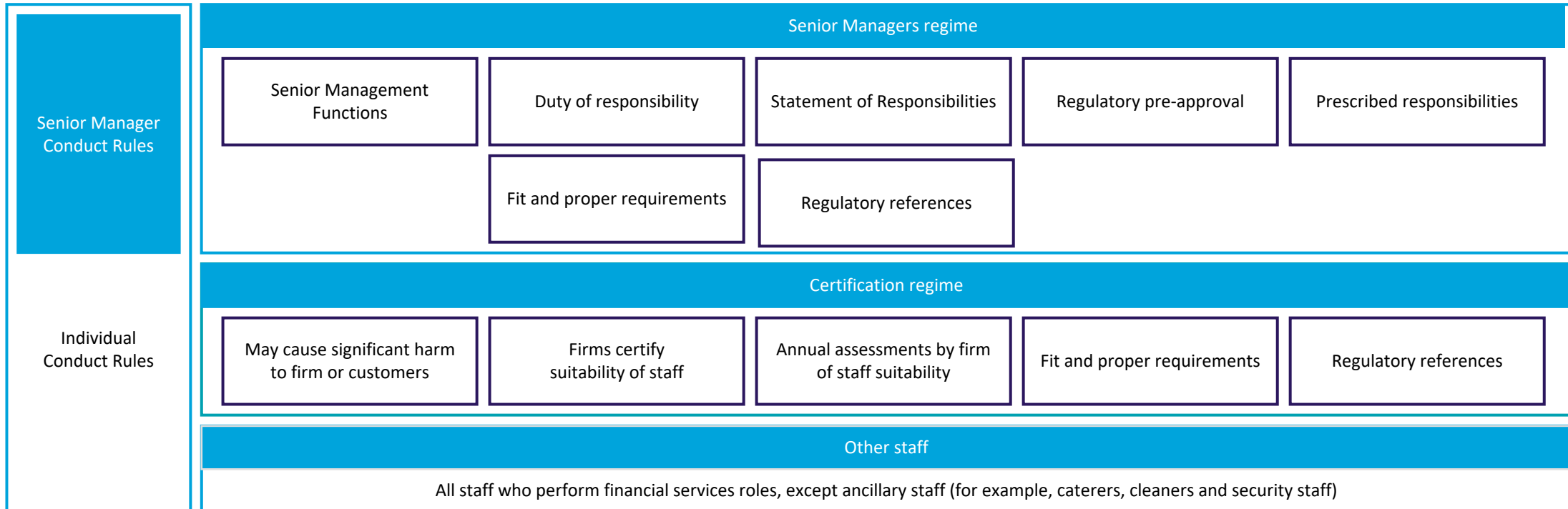
Three elements to the core regime

1. **Senior Managers Regime** – most senior individuals in a firm and will require FCA approval; all Senior Managers must have a statement of responsibility setting out what they are responsible and accountable for; will also have a duty of responsibility so that if anything goes wrong, the FCA can consider whether the individual took reasonable steps; some new responsibilities (**prescribed responsibilities**)
2. **Certification regime** – this is for those individuals who are not senior managers but whose roles could have a large impact on customers, markets or the firm. Are not FCA approved, but firm must check and confirm (ie certify) that they are **suitable to perform their role on at least an annual basis**
3. **Conduct Rules** – these rules will **cover almost every person** who works at the firm and are about improving the behaviour of staff

Three categories of staff

1. **Senior Managers** - Prior regulatory approval, Statement of responsibility, Duty of responsibility, prescribed responsibilities, subject to all new Conduct Rules
2. **Individuals who are not senior managers but could have a large impact on customers, markets or the firm** - Firm certifies as fit and proper; Subject to first tier Conduct rules
3. **Nearly everybody else (ie all staff other than those considered to be ancillary eg receptionists; post room staff; switchboard)** - Subject to first tier Conduct rules

Summary



Who is a senior manager?

- Those individuals who are the most senior in a firm with the greatest potential to cause harm or impact upon market integrity.
- The FCA defines which types of role are Senior Management Functions so it knows who a firm's most senior decision makers are and to ensure firms clearly allocate responsibilities to those key decision makers.
- Individuals can hold more than one function (and can be applied for at the same time). Also, similar to the existing Approved Persons regime, not all functions are applicable to all firms.
- There is no territorial limitation on the Senior Managers Regime. This means that the Senior Managers Regime will apply to anyone who performs a Senior Manager role, whether they are based in the UK or overseas.

The Senior Management Functions

(for core firms)

Function name	Description
Governing Functions	
SMF 1 – Chief Executive	This is the person(s) with responsibility, under the immediate authority of the governing body, for the conduct of the whole of the business (or relevant activities). Note: Although the Chief Executive is the most senior member of an executive team, it does not mean that a firm’s governing body cannot allocate specific responsibilities to other Senior Managers.
SMF 3 – Executive Director	A director of a firm, other than a Non-Executive Director.
SMF 27 - Partner	A partner in a firm, other than a limited partner in a partnership registered under the Limited Partnership Act 1907.
Governing Function – Non-Executive	
SMF 9 - Chair	The person with responsibility for chairing, and overseeing the performance of the role of, the governing body of the firm.
Required Functions	
SM16 – Compliance Oversight	This is the person responsible for the compliance function in the firm and reporting to the governing body on this
SMF 17 – Money Laundering Reporting officer	This is the person who has responsibility for overseeing the firm’s compliance with the FCA’s rules on systems and controls against money laundering.
SMF 29 – Limited Scope Function (relevant to some limited scope firms only)	This is currently called the ‘Apportionment and Oversight Function’ under the Approved Persons Regime. It is the person who deals with the apportionment of responsibilities under SYSC 4.4.3 R and oversees the establishment and maintenance of controls under SYSC 4.1.1 R.

Responsibilities

- **Statement of Responsibilities**

- Every Senior Manager must have a Statement of Responsibilities Document which sets out their role and responsibilities.
- These must be submitted to the FCA when applying for approval/on significant change
- There will be a template provided

- **Duty of Responsibility**

- Every Senior Manager will have a duty of responsibility as a result of FSMA so that they are held accountable if a firm breaches one of the FCA's requirements and they did not take "reasonable steps" to prevent the breach
- Burden of proof lies with the FCA to prove that the Senior manager did not take steps a person in that position could reasonably be expected to take to avoid the firm's breach occurring

Responsibilities

- **Prescribed Responsibilities**

- Specific Responsibilities defined by the FCA which must be allocated to Senior Managers (should be given to the most Senior Manager responsible for that issue)
- For Core forms these are:

Prescribed Responsibility	Description
1	Performance by the firm of its obligations under the Senior Managers Regime, including implementation and oversight
2	Performance by the firm of its obligations under the Certification Regime
3	Performance by the firm of its obligations in respect of notifications and training of the Conduct Rules
4	Responsibility for the firm's policies and procedures for countering the risk that the firm might be used to further financial crime
5	Responsibility for the firm's compliance with CASS (if applicable)
6	Responsibility for ensuring the governing body is informed of its legal and regulatory obligations

Systems and Controls

- **Firms** – will need to ensure they have the systems and controls in place to comply with the new requirements (eg governance procedures, fit and proper processes, allocation of Prescribed Responsibilities)
- **Individuals** – Senior Managers must ensure they understand the nature of their role and the obligations, responsibilities and duties of being a Senior manager

Responsibilities map

Compile and maintain document(s) showing:

- Firm's key functions
- What positions run the firm
- Individuals in each position or with responsibility
- Allocation significant responsibilities
- Reporting lines

The responsibilities map should:

- Be a comprehensive up-to-date document(s)
- Describe management and governance arrangements
- Ensure collective allocation of responsibilities complete
- Detail lines of reporting & responsibility & the persons performing them
- Detail management & governance of firm's main business areas & governance functions

Regulator will use for BAU and will scrutinise during supervision

What do you as an individual need to do?

Your responsibility is personal, not collective

1. Walk through your area of responsibility from nose to tail

- Periodically refresh your understanding of the risks especially as things change
- Is the governance fit for purpose

2. Identify and calibrate the risks

- How do you manage them
- Look at the MI you give and receive

3. Assess operational risk framework

- Check what Compliance monitors
- Does the business get the right messages

4. Review your role (and statement of responsibility)

- Is it clear and up-to-date
- Are your reports suitable and do you oversee them

Responsibility of NEDs

Responsibility of NEDs



Key impact

The shift towards individual responsibility may make it harder to attract and retain Senior Managers.

Employers will want to ensure that the Statement of Responsibilities is detailed and comprehensive while Senior Managers are likely to want to minimise the areas for which they would be held responsible, leading to lengthy negotiations. It is likely that Senior Managers will want to obtain independent legal advice and may look to the employer to cover this cost.

Senior Managers keeping more detailed records of decision making within their business area may fuel a practice of 'finger pointing'.

Exits could become more protracted with Senior Managers potentially threatening to provide unhelpful handover certificates unless their demands for severance are met.

Banks could see an increase in whistleblowing allegations from Senior Managers who are exited to try and minimise culpability and extract exit packages.

In future, a Senior Manager's entry on the FCA database will include more information on disciplinary action taken against them. This could have implications for a manager's future employment prospects.

The new regime may require changes to employment contracts and policies such as ensuring that there is a requirement to comply with the Conduct Rules, complete Statements of Responsibilities and handover certificates and a contractual basis for dismissing with immediate effect where these requirements are not met.

Although much of the focus of the new regime is on Senior Managers, the conduct rules will be extended to cover more employees than the previous regime.

The Certification Regime and other staff

Certified staff ...

Are those staff that:

- are involved in the firm’s regulated activities
 - Are not Senior Managers
 - Are based in UK/deals with UK customers; and
 - Whose activities involve a risk of significant harm to firm or customers
- The FCA has set out the roles it considers to be Certification functions
 - The Significant Management Function applies to those who has a significant responsibility for a significant business unit and is not limited to those that perform commercial activities (so could include HR, IT, Ops)

Certification Function	Overview
Significant Management Function (based on current CF 29)	These individuals perform functions that would have been Significant Influence Functions under the Approved Persons Regime. These important roles can seriously impact the way the firm conducts its business.
Proprietary traders (covered by CF 29)	
CASS Oversight function (current CF 10a)	
Functions subject to qualification requirements	This includes, for example, mortgage advisers, retail investment advisers and pension transfer specialists. The full list is set out in the FCA’s Training and Competence Sourcebook.
The client dealing function (expanded from the current CF 30)	This function will be expanded from the current CF30 function to apply to any person dealing with clients, including retail and professional clients and eligible counterparties. This will cover people who: <ul style="list-style-type: none"> • advise on investments (other than a non-investment insurance contract) and perform other related functions, such as dealing and arranging • deal, as principal or agent, and arrange (bring about) deals in investments • act in the capacity of an investment manager and all functions connected with this • act as a bidder’s representative
Supervisors or Managers of a Certified Function (indirectly or directly) but who is not a Senior Manager	This will ensure that people who supervise certified employees are held to the same standard of accountability. It also ensures a clear chain of accountability between junior certified employees and the Senior Manager ultimately responsible for that area. For example, if a firm employs a customer-facing financial adviser, every manager above them in the same chain of responsibility will have to be certified (until the Senior Manager approved under the SMR is reached).

Fit and proper

Fit and Proper

- Fit and Proper requirements apply to Senior Managers, NEDs, and Certification staff
- Firms must assess an individual's fitness and propriety on an ongoing basis and at least once a year
- Firms must collect new evidence when assessing candidates for these roles including criminal records checks and regulatory references

Conduct Rules

First tier – rules for everybody

Individual Conduct Rules

Rule 1: You must act with integrity.

- Manage risk, exercise sound judgement, observe rules as well as honesty

Rule 2: You must act with due skill, care and diligence.

- Understand the business, the regulations and act compliantly & competently

Rule 3: You must be open and cooperative with the regulators.

Rule 4: You must pay due regard to the interests of customers and treat them fairly.

Rule 5: You must observe proper standards of market conduct.

- All markets, not just listed securities

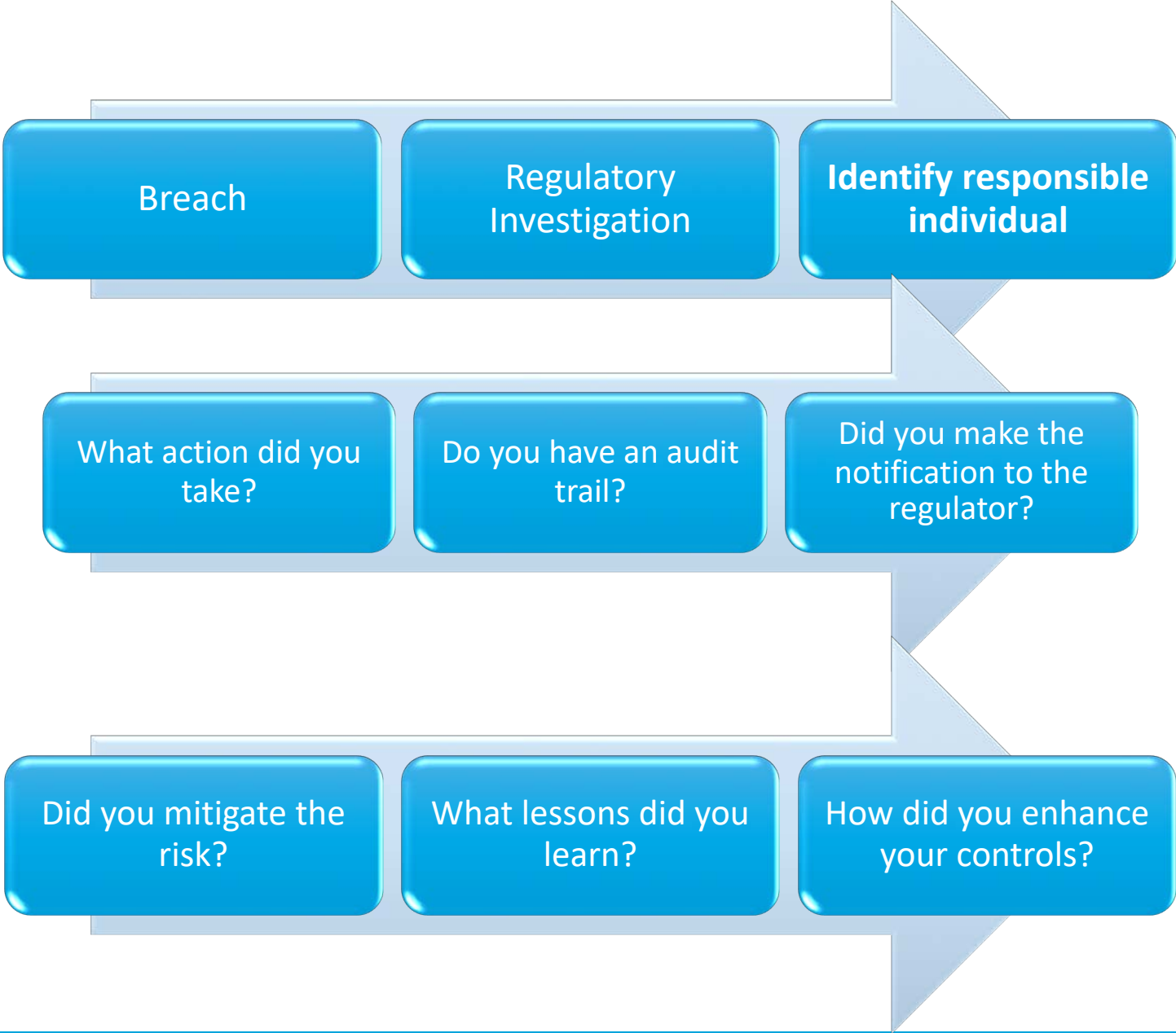
Second tier – Senior Manager Conduct Rules

SC1: You must take reasonable steps to ensure that the business of the firm for which you are responsible is controlled effectively.

SC2: You must take reasonable steps to ensure that the business of the firm for which you are responsible complies with relevant requirements and standards of the regulatory system.

SC3: You must take reasonable steps to ensure that any delegation of your responsibilities is to an appropriate person and that you oversee the discharge of the delegated responsibility effectively.

SC4: You must disclose appropriately any information of which the FCA or PRA would reasonably expect notice.



Thematic reviews and market studies

FCA wholesale insurance market study

- In its 2017/2018 Business Plan, the FCA announced its intention to undertake a wholesale insurance market study, to be completed in 2018/2019.
- The study is *“to ensure that the wholesale insurance market is working well and fosters innovation and competition in the interests of a diverse range of consumers”*.
- The FCA will assess *“how effectively competition is working in these markets, including how firms ensure practices do not create market integrity and conduct risks.”*
- The Regulator will take “appropriate remedial action” following this.

FCA - Value in the distribution chain review

- In its 2017/2018 Business Plan, the FCA further announced that it would carry out a review into value in distribution chains.
- The FCA said that *“Our review into the effectiveness of governance and oversight of delegated authority outsourcing showed that the length of the distribution chain can potentially erode the value of a product or service in different sub-sectors.”*
- Therefore the FCA has stated that it *“...will conduct a further review to understand the end-to-end relationships in these distribution chains. The findings will help us decide whether, and what, further action is required in this sector.”*

FCA – Firms' pricing practices

- In its 2017/2018 Business Plan, the FCA also announced that it would carry out a review into pricing practices.
- First announced in September 2016, when the regulator published a Feedback Statement on its Call for Inputs on Big Data in retail general insurance.
- Intentions for the study include:
 - “..gain a better understanding of how these developments are affecting the market”
 - Looking at “...how firms' pricing approaches and rating factors work in practice”
 - Assessing “...the drivers and types of systems and data [that] firms use to decide the final price to consumers”
- The FCA is concerned that big data might lead to price discrimination rather than price optimisation

Pain points (cont.)



Rising cost of regulation / compliance:

- BIBA: 70% increase in regulation cost for small business brokers
- Accenture: Compliance costs for Financial Institutions will continue to increase over the next two years, driven by regulations and emerging risks
-- (Global Accenture Survey of Executives)
- Thomson Reuters: 63% UK financial firms believe the cost of senior compliance staff will increase in the next 12 months
-- (2017 Cost of Compliance Report)

Greater risk of missing something important due to increased regulatory burden

The screenshot shows the top navigation bar of the BIBA website. The navigation menu includes: Home, Press Releases, BIBA Research Reveals 70% Increase In Regulation Costs For Small Insurance Brokers, Share, Email, 17TH JANUARY 2017. The main content area features a blue header with the text: BIBA RESEARCH REVEALS 70% INCREASE IN REGULATION COSTS FOR SMALL INSURANCE BROKERS.

The screenshot shows the newsroom main page of the Accenture website. The navigation bar includes: < PREV, NEWSROOM MAIN, NEXT >. The main content area features a red header with the text: APRIL 10, 2017. The main headline reads: Compliance Costs for Financial Institutions Will Continue to Increase Over the Next Two Years Driven by Regulations and Emerging Risks, According to Global Accenture Survey of Executives. The sub-headline reads: Firms spending more than 5 percent of net income on compliance jumps 40 percent year-on-year.

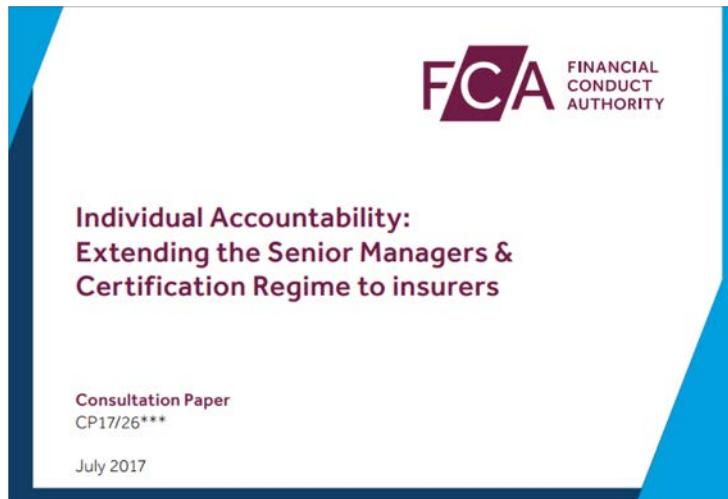
Pain points (cont.)

Business fines

Personal liability for senior execs (SMCR)

Duty of responsibility

Every Senior Manager will have a duty of responsibility¹³. This means that if a firm breaches one of our requirements, the Senior Manager responsible for that area could be held accountable if they did not take 'reasonable steps' to prevent or stop the breach.



This is a screenshot of a news article on the FCA website. The article title is 'FCA fines Towergate and former director Timothy Philip for client and insurer money failings'. The page includes a search bar, navigation tabs for 'About us', 'Firms', 'Markets', 'Consumers', 'News', and 'Publications', and a breadcrumb trail: 'Home / News / FCA fines Towergate and former director Timothy Philip for client and insurer money failings'. It also features a 'Print page' button and social media sharing options for LinkedIn, Twitter, and Email. The article was published on 13/07/2016 and last updated on 13/07/2016.

Wednesday 23 August 2017 11:57am

More than 70,000 City managers could be held personally responsible for misconduct under the FCA's new accountability rules

This is a screenshot of an article from FXMM (Financial eXchange Markets Monitor). The article title is 'FCA and PRA regulatory fines have already quadrupled last year's total'. The article is by Wolters Kluwer and was published on 17 May 2017. It currently has no comments. The article text states: 'The number of fines issued against individuals has exceeded those issued against organisations for the first time, putting the focus on senior managers once more...'. The article has 73 shares.

Reg Tech Solutions

- ▶ Continually updated with regulatory expertise
- ▶ Multi-device (web, tablet, mobile)
- ▶ Cost-effective - *cost of compliance is a heavy burden on the industry, somewhere between £10 billion and £20 billion in the UK*
- ▶ Secure
- ▶ Increasing the effectiveness and the efficiency of compliance
- ▶ Increased bureaucracy damages customer retention and onboarding, while complex regulation can get in the way of innovation
- ▶ Can be applied across different areas of the business



QUESTIONS?
