Financial Conduct Authority

Regulator Assessment: Qualifying Regulatory Provisions

Title of proposal: TR15/6 - Handling of insurance claims for Small and Medium-sized Enterprises (SMEs)

Lead regulator: FCA

Date of assessment: April 2017

Commencement date: May 2015

Origin: Domestic

Does this include implementation of a Cutting Red Tape review? No

Which areas of the UK will be affected? Whole of UK

Brief outline of proposed new or amended regulatory activity

The thematic review was undertaken to assess how property claims made by SMEs were handled. It was not intended as an assessment of the degree to which firms complied with the rules in ICOBs in relation to claims, these rules being both brief and high level. The review included research among SMEs to understand their experience of how their claims had been handled.

The report on the findings of the review highlighted a number of areas where firms needed to enhance their processes to better meet claimants' expectations. However in only two areas did our report set out expectations which went beyond existing rules and guidance:

- our customer research highlighted aspects of the handling of claims which were particularly important to SMEs – for example guidance on how to mitigate the loss, an action plan setting out what will happen and who is responsible, proactive communication about the progress of the claim, speedy payment of claims. We set these out in the report and they can be regarded as providing more detail beyond the provisions of ICOBS

- the need to have in place processes to capture claimant feedback to determine whether the claimants were being treated fairly.

Which type of business will be affected? How many are estimated to be affected?

The affected businesses will be insurers which provided insurance for SMEs. This is a relatively concentrated market with 10 insurers writing 75% of this business[1]. We do not have data on precisely how many insurers write SME insurance, but as regards the broader category of

[1] Source: Verdict Financial 2016 SME insurance Survey

Commercial Insurance 36 insurers have a market share of a quarter percent or more. It is reasonable to assume that, with a market share of commercial insurance of 0.25% or more, most of these firms will write SME insurance to some degree, including where underwriting authority is delegated to another party – a broker or a managing general agent (MGAs – intermediaries which function as underwriters).

Price base year	Implementation date	Duration of policy (years)	Business Net Present Value	Net cost to business (EANDCB)	BIT score
2015	2015	10	-19.94	2.3	11.5

Please set out the impact to business clearly with a breakdown of costs and benefits

Note – for all cost estimates below we have assumed the changes will be applied by experienced compliance staff at an estimated rate of £48/hour. The 2016 Robert Half salary guide estimates that a compliance manager in the risk and compliance function of a financial services company based in London earns between £70,000 and £104,000 per annum. Based on working 8 hours per day for 260 days each year our rate equates to £100,000 per annum and is therefore considered a suitably prudent figure for the purposes of our estimates.

Familiarisation costs

The report is 6060 words long which, at a reading speed of 100 words a minute[2], would take 1 hour and 10 minutes to read. It is reasonable to assume that 3 people per firm – 2 in claims and 1 in compliance – will need to read the report. Over 36 firms this equates to **119 hours x £48 = £6k.**

In addition to reading the report a summary of it and a gap analysis – comparing the findings to a firm's processes and procedures – will need to be prepared for consideration by committees and boards. It is assumed that this will take one FTE two days per firm. The costs of preparing the gap analysis will therefore be **£28k (16 hours x 36 firms x£48 per hour)[3].**

No additional costs have been included for consideration by committees and boards of the gap analysis as this is considered part of business as usual in regard to ongoing consideration of regulatory risk within firms.

Total familiarisation costs = £34k

Remediation costs

We asked four insurers to provide information about the incremental costs they would incur in implementing the findings of the review, in the two areas where the report went beyond existing guidance. Three of the firms had been included in the review, one had not. The four firms were chosen to provide a representative cross-section of insurers participating in the SME market. In particular they varied by business model – for example as to whether underwriting/acceptance of risks was undertaken directly or delegated – and the degree to which our engagement with them indicated they needed to take remedial action. As such is reasonable to assume the costs are representative and we would not expect them to be significantly higher or lower than other insurers. We asked the four firms to provide information on: one-off costs, ongoing costs and any cost saving. Their responses were:

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[2] EFTEC (2013), "Evaluating the cost savings to business from revised EA guidance – method paper".

[3] We arrived as this estimate based on our broader supervisory knowledge of how firms respond to our Thematic review and also on supervisory conversations with firms about their procedures relating to this specific issue

Firm	One-off costs (£k)	On-going costs (£k) per annum	Cost savings - ongoing(£k)
Firm 1	20	nil	
Firm 2	122*	15	
Firm 3	116	90	50
Firm 4	Nil**	175	
Mean	65	70	12

* One-off costs include £40k, over three years, to complete survey of SME claimants.
** All additional costs are projected to be incurred every year

Virtually all the incremental costs firms are incurring are in relation to capturing claimant feedback and monitoring their claims experience. These costs fall into two categories: i) the actual surveying of claimants ii) the need for additional staff to analyse these results.

The costs savings of one firm will result from payment of claims by BACS rather than cheque.

The analysis of the responses from the four insurers indicates that the additional costs they will incur are not correlated to market share. (The market shares of the four firms varied markedly but are not show here because this would allow individual firms to be identified.)

Rather the main driver of the size of the incremental costs appears to be how far from the standards set out in our report the insurer was at the time of publication of our report. Therefore it is reasonable to assume that, on average, the additional costs of the 36 insurers with a market share of 0.25% of more will equate to the mean of the four firms surveyed.

Therefore the remediation costs for the 36 insurers are:

One-off costs **£2.34m (36 x £65k)**
Ongoing costs for 10 years **£2.01m (36 x £58k (£70k less £12k)**

Total one off costs (familiarisation and remediation) = £2.64m
Total ongoing costs: £2.01m per year

The aim of this measure is to be beneficial to wider SMEs but we have been unable to quantify the direct benefits some of which may be indirect. Given this is a retrospective assessment we do not consider it proportionate to carry out a data collection exercise.

Please provide any additional information (if required) that may assist the RPC to validate the BIT Score.