

25 May 2022

**Dear Board of Directors****FCA Supervisory Strategy for Personal and Commercial Lines Insurance Intermediaries (P&CLII)**

We are writing to you to set out our view of the key risks Personal and Commercial Lines Insurance Intermediaries could pose to their consumers or markets. Please consider the extent of these risks in your business and act where you identify harm.

**Who this letter applies to**

This letter is for firms in the Personal and Commercial Lines Insurance Intermediaries portfolio. This includes:

- General insurance intermediaries serving retail and/or commercial customers,
- Loss assessors and
- Firms for which broking of insurance products is ancillary to their primary business

**Our view of the portfolio**

Our view of the General Insurance Intermediary sector overall is that there are significant risks of potential harm that both the market and individual firms need to address. We want to see a market where customers are appropriately supported both in purchasing the right insurance products for their needs, and when they need to claim. We want to see products sold that offer fair value to consumers, and for there to be strong systems and controls within firms.

We continue to believe that the most significant risk of harm in the portfolio is through customers buying unsuitable or poor value products, we frequently see examples of harm caused by mis-selling, where firms lack customer-centric cultures and where consumer outcomes have not been appropriately considered. We also continue to observe ineffective governance and control arrangements.

We will continue to review firms' regulatory returns, including annual pricing attestations together with other sources of information to target our supervisory work and to take appropriate intervention where we identify such concerns.

Despite these harms, we have also observed some notable examples where intermediaries have supported their customers, including through the claims process. We highlight the support provided with business interruption and weather-related incidents as two good examples of this.

We published our [business plan](#) on 7 April 2022, which explains how we see our future role and priorities, how we intend to deliver them, and how we will measure our performance. The harms identified for this portfolio resonate with some of the key themes identified within the business plan and we encourage you to read it alongside this letter.

## **Governance and oversight**

We wrote to the portfolio in [September 2020](#) noting that many of the key harms were linked to poor governance and controls. It is disappointing to note that we continue to see evidence of consumer harms where we can attribute the failings to poor governance or insufficient focus on good consumer outcomes.

We would remind the portfolio that good governance is central to the effective running of any financial institution. Some critical components of good governance include:

- clear accountabilities for activities which affect outcomes, with appropriate channels of escalation
- a robust risk framework which identifies key risks of harm, which is appropriately monitored and mitigated by accountable individuals
- strong and independent Board oversight and challenge (where applicable)

## **Key risks**

### **Pricing practices and value for money**

*Firms must have processes in place to deliver products that are fair value to customers. This should be underpinned by robust governance over pricing decisions to fully consider customer outcomes and improve pricing transparency and to ensure that their policies do not discriminate against certain demographics of society.*

Our work on pricing practices highlighted that price walking leads to significant risks of harm to customers. We also found that firms' pricing governance and control frameworks do not allow firms and senior managers to effectively oversee their pricing practices and activities.

We published the final report on our pricing practices market study in September 2020 and updated it in May 2021 in Policy Statement [PS21/11](#). In this we outlined our proposed package of rules to tackle the harms identified, which have now taken effect.

We expect firms in this portfolio to have fully implemented these rules alongside an oversight framework which ensures continuous compliance and consideration of customer outcomes. Senior managers will be required to provide an annual confirmation that their firm has complied with the requirements in ICOBS 6B. This requirement will help us to hold firms and individuals to account for ending price walking for home and motor insurance.

We will test and review how firms have implemented the required changes through market intelligence, regulatory returns data and reporting. We expect firms to report breaches to us in a timely manner in line with the SUP 15 and Principle 11 requirements.

We continue to see instances of harm occurring due to firms' ineffective oversight of remuneration within the distribution chain, including via appointed representatives. The use of high commission and administration fees by firms acting as product distributors can significantly inflate an insurance premium which can lead to customers receiving poor value for money.

An example of this is the insurance of high-rise residential buildings. In our letter, issued 28 January, regarding [insurance costs for multi-occupancy buildings](#), we highlighted that the significant increase in costs being passed on to residential leaseholders, is contributing to the financial difficulties that many such customers are experiencing.

Our proposed Consumer Duty also provides additional obligations for firms to ensure that their products and services are fit for purpose and offer fair value. Our Consultation Paper [CP21/36](#) proposes draft handbook rules to underpin a new Consumer Principle that provides an overarching standard of conduct for all retail focused firms that we regulate.

We will work closely with firms and their trade bodies during the Consumer Duty implementation period to help identify and work through examples of good and poor practice that assist stakeholders to apply the Consumer Duty.

Our new pricing practices and product governance rules represent a step change for the insurance industry. We expect senior managers and Boards (where applicable) to have delivered these regulatory changes effectively and to be fully engaged on issues related to value and pricing. Firms should have embedded these changes so that they can evidence that customers receive value from the products they hold and should be subject to ongoing review.

Where we identify firms and the accountable SMF have not complied with the requirements of these rules, we will intervene at pace and look to take appropriate action which includes referring the matter to our Enforcement Division where necessary.

## **Product oversight and governance**

*Customers should receive insurance products that meet their demands and needs and deliver fair claims outcomes. Firms need to ensure that contract terms are not ambiguous and that customers receive the appropriate information that is clear, fair and not misleading to enable them to make an informed decision.*

We continue to see customers buying products which do not always offer fair value and provide insufficient cover at the point of claim. There is also a risk that a lack of clarity, from ambiguous contract wordings could lead to customers purchasing insurance that does not provide the level of cover expected. We highlight business interruption as an example where this risk has been prevalent, but we are concerned that the issue may be more widespread and exist in other products.

We recognise that firms in this portfolio can be manufacturers, distributors or both, within the context of a distribution chain. Intermediaries that act as manufacturers (i.e. creating, developing, designing and/or underwriting a contract of insurance) should undertake regular checks of their products to ensure that consideration is given to the best interests of customers/consumer outcomes. This should be embedded within every stage of the product lifecycle and be supported by robust product oversight and governance arrangements.

Manufacturers should carefully identify their target market for products and ensure that distribution methods are appropriate and that products reach the intended target market. Intermediaries that are product distributors need to understand the intended value of products and ensure that their distribution arrangements (including remuneration) are consistent with providing fair value to the customer. Firms need to give due regard to the financial promotion rules particularly to ensure that financial promotions are clear fair and not misleading. There should be effective oversight of the distribution chain including any appointed representatives.

We are planning a broad supervisory programme of work, which will be supported by increased use of analytics to review firms' reporting data, to measure compliance with the rules, identify consumer harm, and monitor the market.

## **Client assets and orderly wind down**

*Firms who hold client assets must comply with the rules set out in the Client Assets Sourcebook (CASS) to help ensure client money is appropriately protected and that if the firm fails, they are returned as quickly, and as whole, as possible. Firms need to adhere to their financial resource requirements so that they can conduct business,*

*wind down and, where applicable, fail without causing significant harm to consumers and market participants.*

We identified from our financial resilience surveys and subsequent supervisory interactions, that a substantial number of firms have inadequate CASS arrangement and insufficient oversight and control of their client money arrangements.

Safeguarding client money is a fundamental requirement and requires SMF oversight. We expect firms that hold client money to have rectified the issues identified in our [Dear CEO letter](#) of July 2021, maintaining adequate client money arrangements. Principle 10 of the FCA's Principles for Business states a firm must arrange adequate protection for clients' assets when it is responsible for them. We take failure to comply with the Principles for Business and the CASS rules seriously. When misconduct is identified, we will take appropriate regulatory action.

During the pandemic, many firms experienced issues in maintaining adequate liquidity to manage short term demands on their capital. As a result, we saw a number of firm failures. We are concerned that firms do not adequately consider or plan for orderly wind-downs of their businesses. We expect firms to maintain up to date wind-down plans, specific to their business and operating models, with appropriate triggers for action, so that they can be effectively executed to ensure that minimal harm is caused to consumers and the market when they do exit; this is highlighted in our latest [business plan](#) published on 7 April 2022.

We also expect firms to adopt a prudent approach to the management of their financial resources. We encourage firms to review the observations and consider incorporating our recent findings published in our Thematic Review [TR22/1](#) into their own wind-down planning processes and documents, in a way that is proportionate to the nature, scale and complexity of the firm's activities.

## **Additional Considerations**

***Diversity and Inclusion (D&I) & Environmental Social and Governance (ESG) Considerations:*** It is encouraging to see that D&I and ESG are increasingly on firms' agendas. However, there is still a long way to go before the UK insurance market becomes a truly diverse and inclusive sector; representative of the society it serves. There is growing evidence that diversity of thought, when part of an inclusive culture, supports better decision making by firms. We consider that more diverse and truly inclusive firms will benefit from better risk management and we recognise that D&I is a key component of ESG, both in its own right and as an enabler of creative solutions to other environmental and social challenges. Our expectations in this regard will be proportionate and depend upon both the relative size of a firm as well as the customers you engage with.

In July 2021, we published [DP21/2](#) which engaged in a wide conversation on D&I. In Quarter 3 2022, we will be consulting on proposed new rules and guidance.

***The Senior Managers and Certification Regime ('SM&CR')***: SM&CR aims to establish healthy cultures and effective governance in firms by encouraging greater individual accountability and setting standards of personal conduct. This includes developing a culture for staff at all levels to take personal responsibility for their actions and making sure firms and staff clearly understand and can demonstrate where responsibility resides.

To ensure that our principles and rules are being followed firms should ensure that their Senior Management Function (SMF) holders are aware of their responsibilities. We will hold these individuals accountable where they fail to take reasonable steps to ensure adequate governance, systems and controls, compliance or fail to treat customers fairly.

***Cyber threats & operational resilience***: Given the current heightened international tensions, firms should pay particular attention to their cyber security and must ensure that they proactively manage any operational resilience exposure and take appropriate steps, including the necessary investment, to implement any remedies and address any gaps that may exist within their current arrangements. For reference, in March 2021, we published our Policy Statement [PS21/3](#) Building Operational Resilience in partnership with the Bank of England and the PRA. This introduces final rules and guidance on requirements to strengthen operational resilience in firms. These rules will be applicable to some firms in this portfolio and we are seeking a reduction in the impact (scale, severity, time to remediate) of operational disruptions to firms' important business services.

***Regulatory Responsibilities***: All regulated financial services firms must comply with our rules as set out in the FCA handbook.

We expect all firms within the P&CLII portfolio to be able to show consistently that fair treatment of customers is at the heart of their business model and have an open and cooperative approach both with their customers as well as with the FCA. We will take appropriate action where we find this is not the case.

We would also remind firms of Principle 11 – *"A firm must deal with its regulators in an open and cooperative way and must disclose to the regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice"* and their obligation to engage with us and report matters that have (or could have) serious regulatory or customer impacts. Such notification obligations enable us to not only monitor firms' and individuals' compliance with the rules but also enable us to react quickly to situations that require a regulatory response.

**Oversight of Appointed Representatives:** We would remind firms that act as Principals of Appointed Representatives (ARs) of their ongoing obligation to provide adequate oversight for firm or person(s) for which they remain responsible and accountable. As noted in [CP21-34](#), we consider there is now considerable evidence of harm, including mis-selling, requiring regulatory intervention. Our consultation has now closed and we will be issuing a Policy Statement in due course which firms in this portfolio should pay close attention to. Our proposed rules and guidance are intended to:

- clarify and strengthen principals' responsibilities and our expectations of them
- increase the amount and timeliness of information we receive on principals and their ARs
- Continue work with the Treasury on the outcome of its Call for Evidence on the AR regime as it considers possible legislative change.

**Post-sale verification:** We have also become aware of firms carrying out certain post-sale engagement to verify information provided during the original sales process, which may in certain circumstances expose customers to poor outcomes and potential financial detriment, for example, where the questions and information disclosures during the sales journey were not sufficiently clear, fair and non-misleading. The ICOBS 2.2R requirement on firms to communicate with customers in a clear, fair and non-misleading manner applies to all customer communications including pre-sale questions and disclosure. ICOBS 5.2R also requires that a firm must only propose a contract of insurance that is consistent with a customer's demands and needs. We expect firms to be mindful of these rules, Principle 6 (treating customers fairly) and our other conduct rules both during the sales journey and throughout the life of the policy, including in relation to any verification process. The verification process is not a substitute for appropriately clear pre-sale questioning, and it does not take away the firm's responsibilities to ask the right questions and assess the customers' demands and needs before offering the product for sale.

**Keeping up to date with FCA developments:** We also expect you to monitor our website, and where relevant act on any information relevant to your business that we publish. We encourage you to sign up to [Regulation Round-up](#), our monthly newsletter to firms which highlights topical subjects, events and sector news.

## **Next steps**

We will continue to engage with P&CLII firms in 2022 and 2023 through our planned programme of work. We will write to you again towards the end of 2023 to provide our updated view of the key risks firms in this portfolio pose, the extent to which these risks are being mitigated, and our updated supervisory plans as a result. We expect firms to keep up to date with regulatory developments generally and with the areas covered in this letter.

If you have any questions, please contact your normal supervisory contact or call our firm contact centre on 0300 500 0597. This is the primary point of contact for your firm's day-to-day interactions with the FCA. Further details of how we can be reached are available on our website at <https://www.fca.org.uk/contact>. However, we recognise that there may be occasions in which your firm faces urgent issues of strategic importance. In such significant circumstances, if I am not available, please contact the Head of Department responsible for the P&CLII Portfolio, Lisa Sturley at [Lisa.Sturley@fca.org.uk](mailto:Lisa.Sturley@fca.org.uk).

Yours sincerely

Matt Brewis  
Director