

5 September 2018

## HT 2018-10 ICS updates Compliance Manual in line with IDD changes

The Insurance Distribution Directive (IDD) which replaces the Insurance Mediation Directive sets the baseline for the regulation of insurance distributors throughout Europe. It will have significant impact on all UK insurance firms regardless of the outcome of the Brexit negotiations.

The FCA published its "near-final" rules and guidance to implement the IDD in a Policy Statement (PS18/1) earlier this year and these come into effect from 1 October 2018. Firms may make the relevant changes in advance, but there is no transition period beyond that date.

This article reminds insurance intermediaries of the key IDD implementation issues (previously covered in ICS Hot TopICS) and indicates where updated guidance and template documentation can be found in the ICS Compliance Manual.

### IDD general principles

The IDD introduced these three general principles that apply to all insurance distributors:

**1. To act honestly, fairly and professionally in the best interests of their customers.**

Known as the customer's best interests rule and incorporated into ICOBS, this is both a cultural and procedural issue for insurance distributors building on the principle of treating customers fairly. This principle overarches many of the more detailed conduct of business requirements.

**Section 3.1 and its sub-sections**

**2. To communicate in a way which is clear, fair and not misleading, and to ensure that marketing materials are clearly identifiable as such.**

This reflects an existing FCA principle but there is an added obligation on firms to ensure customers are able to readily identify any promotional material they may see.

**Section 3.7.3**

**3. Remuneration of a distributor or its employees, and performance management of employees, must not conflict with the duty to act in the customer's best interests.**

This means, for example, that firms must not make any arrangements by way of remuneration, sales target or otherwise that could provide an incentive to itself or its employees to recommend a particular contract of insurance to a customer when they could offer a different insurance contract which would better meet the customer's needs.

**Sections 3.2.7.4 and 4.4 - download document T&C14 is an updated example of a firm's remuneration policy**

### Staff knowledge and ability

All those directly involved in insurance distribution (including personnel of a firm's Appointed Representatives) are to undertake at least 15 hours of continuing professional development (CPD) each year. This will include sales staff whose role may be limited to, for example, script-based sales - but their CPD can be tailored accordingly. The FCA has also set out minimum knowledge criteria to cover areas such as products, the claims process, complaints procedure, and insurance regulation. In addition, firms must establish, maintain and keep appropriate records to demonstrate compliance with employee knowledge and ability requirements.

**Part 4 Training and competence - this section and its associated download documents have been substantially revised. New download document T&C17 is an example of an employer's CPD control sheet which may assist with monitoring employees' CPD activity.**

### Status disclosure and scope of service

In addition to the existing pre-contract disclosure requirements, firms must state:

- that they are intermediaries (rather than insurers)

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- whether they are providing a personal recommendation
- whether they are acting on behalf of the customer or the insurer or both (if both, state roles)
- if they have "10% or more" of the voting rights in an insurer (the current rule says "more than 10%").

Such information may be included in client Terms of Business Agreements.

Firms that are under a contractual obligation to distribute exclusively with one or more insurers must state who those insurers are. Where this is not the case and firms do not give a personal recommendation on the basis of a fair and personal analysis they must provide the customer with the name of those insurers they may and do conduct business with.

For products sold to consumers, firms will also have to state whether they are giving:

- a personal recommendation but not on the basis of a fair and personal analysis; or
- other advice on the basis of a fair analysis of the market; or
- other advice not on the basis of a fair analysis of the market; or just information.

**Section 3.2.3 and its sub-sections and download documents have been updated including the download document SP06 - Terms of Business Agreement.**

### **Demands and needs**

Firms must only offer customers products that are consistent with their demands and needs. This means that firms must establish at the outset what those demands and needs are. This also helps to ensure that customers only buy policies under which they are eligible to claim benefits.

As at present, a demands and needs statement must be provided to the customer for each product sale, including renewal. For advised sales, firms must provide the customer with a personalised explanation of why a particular policy would best meet their demands and needs.

**Section 3.2.4 and its sub-sections.**

### **Product disclosure and the IPID**

The obligation for firms to provide appropriate information about a policy in good time and in a comprehensible form so that customers can make an informed decision about the arrangements proposed remains unchanged. But product manufacturers must now provide a standardised "Insurance Product Information Document" (IPID), similar to a Key Features Document or Policy Summary for each non-life consumer product. The client-facing firm will generally issue the IPID to the customer before the conclusion of the contract along with any other information required to facilitate the customer's "informed decision".

Firms are also expected to consider providing a summary containing the IPID information for *commercial* customers and to cooperate with all partners in the distribution chain to ensure the customer information needs are met. They should also consider at which point in the sales process the information they are providing will be most useful to the customer to enable them to make an informed decision.

**Section 3.2.5 and its sub-sections.**

### **Remuneration disclosure**

Firms must disclose the nature and basis of the remuneration they receive relating to the insurance contract. 'Nature' involves the type of remuneration such as basic commission, bonus, profit commission or other financial incentive. 'Basis' involves the source of the remuneration; e.g. from the insurer. The actual amount of the remuneration need not be stated except on the request of a commercial customer (or a consumer in relation to the firm's fiduciary duty).

This disclosure should cover all remuneration which the firm receives or may receive in relation to the distribution of the contract of insurance, whether it is provided indirectly by the insurer or another firm within the distribution chain. It should include financial or non-financial benefits paid, for example, by way of a bonus for achieving a certain sales target.

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This does not alter the existing obligation for firms to state up-front the exact amount of any fees to be paid by the customer (consumer or commercial) at the outset or at any other time - such as charges for mid-term adjustments, administration and cancellation.

**Section 3.2.3 and its sub-sections.**

## **Means of communication**

Firms can provide the necessary disclosure information to customers in a durable medium other than paper or via a website that meets certain conditions. The customer must make an active and informed choice and give consent to receive the information via a website. A paper copy must be sent on a customer's request, free of charge. A customer's existing choice or consent to receive the information by means other than paper, can be carried through at renewal if that is in context with the transaction but firms must inform the customer of the option to receive the information in a different form (for example, by clearly mentioning the option in the renewal notice).

**Section 3.2.4.3.**

## **Conflicts of interest**

Firms must establish and maintain an effective conflicts of interest policy. The types of conflicts of interest that arise or may arise must be assessed and an up-to-date record kept of conflicts which have arisen or may arise. These must be reported to management at least annually. Disclosure of conflicts to customers should be made only when the arrangements established to manage conflicts of interest are not enough to ensure, with reasonable confidence, that risks of damage to the interest of the customer will be prevented.

**Section 1.8 and its sub-sections; updated download document COI01 offers a basis for a firm's conflicts of interest policy.**

## **Professional indemnity insurance**

The minimum level of professional indemnity insurance or a comparable guarantee is increased to €1,250,000 per claim per year, and €1,850,000 per year in aggregate for all claims. These figures are not a recommendation or advice as to what is needed and each firm must determine what level of PI cover is needed to meet its own specific circumstances.

**Section 2.2.**

## **Complaints**

Firms must have procedures in place for dealing with a complaint from any customer, not just those eligible to use the Financial Ombudsman Service (FOS). ICS has always recommended that firms' complaints procedures encompass all forms of complaint and no specific changes have been made to the Compliance Manual.

**Section 3.3.2.**

## **Product oversight and governance (POG) arrangements**

Product manufacturers (usually the insurers) must clearly identify their target market and carry out product analysis and reviews to check performance and potential consumer detriment. They must also justify and monitor distribution channels and provide appropriate information on the product to distributors. Distributors (including insurance intermediaries) need to be clear about their product distribution arrangements, which includes establishing processes and procedures for the products they intend to distribute, obtaining all relevant information from the manufacturer and defining a distribution strategy.

**New Section 3.8 and its sub-sections; download document POG01 is a product oversight and governance policy and POG02 is a product design approval process to assist firms that are product manufacturers.**

## **Perimeter**

Following the IDD and government action the FCA has made some changes to its Perimeter Guidance (PERG 5) to reflect certain changes to the scope of regulation. This may affect some aspects of insurance distribution.

**Section 5.6 has been updated and now includes sub-sections on The Business Test, Exclusions from regulation, Ancillary Insurance Intermediaries and Passporting.**

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## What do we need to do now?

If you have not already done so, you will need to review your processes, procedures and documents to ensure they meet the new requirements.

Particular attention should be paid to:

- Staff training and CPD including for any appointed representatives\*
- Sales procedures including disclosure of status, scope of service and remuneration
- Documentation provision including terms of business, demands and needs statements, product disclosure (including via IPID), and making paper versions available free of charge
- Marketing material
- Conflicts of interest and staff remuneration policies
- Professional indemnity limits
- Product oversight and governance

**Note: this list is not exhaustive**

\*The ICS E-learning facility provides easy access to over 200 compliance, insurance and business skills courses and the system automatically creates individual CPD records and evidence of any external CPD activities can be added manually. Managers and supervisors are able not only to set learning plans for staff members or groups of staff but also to monitor the progress of individuals and schedule regular reports.

To enquire about a free trial of the E-learning facility please call us on 01892 539600 or email [admin@insurancecompliance.co.uk](mailto:admin@insurancecompliance.co.uk).

ICS has also produced a powerpoint presentation which firms can use when undertaking IDD training with staff. This can be found in section 3.2.13 and 3.8.8 of the ICS compliance manual.

## Further information

FCA website: PS18/1 Insurance Distribution Directive implementation: <https://www.fca.org.uk/publications/policy-statements/ps18-1-insurance-distribution-directive-implementation-feedback-and-near-final-rules>

**If you would like any help or information on the IDD requirements or any other FCA regulation issues, ICS Services, e-learning or anything else we might be able to assist you with, please contact your usual ICS representative, Head Office on 01892 539600 or [admin@insurancecompliance.co.uk](mailto:admin@insurancecompliance.co.uk)**