IUA GOOD PRACTICE GUIDANCE FOR DELEGATED AUTHORITIES

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FOREWORD BY DAVE MATCHAM

Delegated authorities are an increasingly popular business model for many members of the International Underwriting Association. Our London Company Market Statistics Report quantified the amount of business written in this way at close to £4bn in 2019.

The term can refer to a number of different arrangements but principally involves the outsourcing of certain functions by an insurer. It can be applied throughout the insurance product cycle, from risk assessment and underwriting to claims payment.

Such set-ups can offer significant benefits for both parties to a contract and help establish more competitive markets. They enable companies to provide services locally without the need to establish their own expensive infrastructure. Clients, meanwhile, are provided with greater access to capital and expertise. Coverholder firms can develop considerable knowledge in niche product areas, or geographical regions and develop excellent local relationships.

In order for delegated authority arrangements to work successfully, however, it is important that companies properly assess the functions to be outsourced, choose the right partners to operate with and exercise appropriate oversight. They must understand the responsibilities they continue to have to clients and comply with relevant regulations.

This Good Practice Guidance, produced by the IUA's Delegated Authority Underwriting Group, seeks to address these issues and others. I hope you find it useful.

Dave Matcham

Chief Executive

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GOOD PRACTICE GUIDANCE – DELEGATED AUTHORITY (Second Edition)

This guidance provides an introduction to delegated authority in the company market and sets out practical guidance for insurers in assessing new Coverholders, managing binding authority contracts and renewing such contracts. Guidance is also provided on delegated claims and complaints handling and Coverholder run-off procedures.

Where applicable, the guidance highlights the relevant FCA/PRA requirements and guidance for outsourcing, including the provisions at SYSC 3.2, SYSC 8 and SYSC 13. In addition, other requirements have been considered, including Solvency II outsourcing requirements and the findings of the FCA's thematic review of delegated authority in 2015.

The guidance has been drafted with regard to the applicable regulatory rules and is intended to support compliance with those rules as they apply at the date of this guidance. Nevertheless, it remains the obligation of firms and Coverholders at all times to ensure that they are aware of and comply with any regulatory rules to which they are subject.

In the second version, the guidance has been updated to take into consideration the implementation of the Insurance Distribution Directive (IDD) in 2018 and subsequently, the findings of the FCA's thematic review of general insurance distribution chain and Dear CEO letter in 2019, in addition to areas highlighted by the FCA's enforcement activity in this space. Amendments have also been made in light of Brexit, although much of the guidance from the first edition remains relevant.

This guidance has been produced for those involved in delegated authority business. It summarises the key points for firms to consider when operating delegated authority business. It is very important to emphasise that it has been designed to inform firms of some of the points they may need to consider, and is not intended to be a complete statement of the law, market practice or a prescriptive list of requirements which a firm must adhere to. Firms will need to refer to their own company procedures and compliance requirements. It should not be relied on or be used as a substitute for legal advice in relation to any particular set of circumstances. Accordingly, the IUA does not accept any liability for any loss which may arise from reliance on this publication or the information it contains.

Please note that firms should also take into consideration any local laws or regulatory requirements in the country or jurisdiction applicable to business being conducted.

Note on insurer firms with dual platforms:

Please note that where firms operate a dual platform (operate a Lloyd's market stamp in addition to a company market stamp), insurers will also need to consider any Lloyd's requirements. All Lloyd's requirements are available at https://www.lloyds.com/.

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SECTION 1 - INTRODUCTION TO DELEGATED AUTHORITY

1.1 Introduction

Please note that references to insurance(s), insurer(s) and insured(s) should be interpreted as also applying to reinsurance(s), reinsurer(s) and reinsured(s), except where expressly stated.

1.1.1 What is "Delegated Authority"?

Delegated authority refers to an arrangement under which an insurer delegates its authority to a company or partnership to enter into contracts of insurance on behalf of the insurer.

1.1.2 How can an insurer delegate authority?

The term 'delegated authority' is widely used in the general insurance industry to describe a variety of arrangements. At the core of these arrangements is external delegation by insurers, involving the outsourcing of functions to intermediaries and other third parties. This is often accompanied by the allocation of other related functions between the parties involved. Outsourcing and any accompanying allocation of functions can take many different forms. It can relate to all stages of an insurance product life-cycle, from product development through to underwriting, distribution and sales and claims and complaint handling.

Delegation is a feature of the way that parts of the general insurance market operates. The term 'delegation' is frequently used by firms where outsourcing is taking place. The FCA Handbook defines outsourcing as 'the use of a person to provide customised services to a firm' (other than a member of the firm's governing body or an individual employed by the firm) or 'an arrangement of any form between a firm and a service provider by which that service provider performs a process, a service or an activity which would otherwise be undertaken by the firm itself'. This means that external delegation of underwriting authority and other significant functions such as claims and/or complaints handling is by definition outsourcing and subject to the relevant requirements in the FCA Handbook.

What is a Coverholder?

"Coverholder" means a company or partnership authorised by an insurer to enter into a contract or contracts of insurance to be underwritten by the insurer. Such contracts will be managed by the "Coverholder" in accordance with the terms of a binding authority. The most common method is to delegate authority to a "Coverholder" under the term of a binding authority contract. However, other forms of delegation are also addressed in this guidance.

What is a binding authority?

A "binding authority" is an agreement between an insurer and a Coverholder which details the terms under which the insurer will delegate its authority to the Coverholder, to enter into a contract or contracts of insurance to be underwritten by the insurer.

A binding authority agreement can also be used to give a Coverholder the authority to issue insurance documents on behalf of insurers. Insurance documents include certificates of insurance, temporary cover notes and other documents acting as evidence of contracts of insurance.

The binding authority agreement will also set out the Coverholder's other responsibilities, such as handling insurance monies, settling complaints or agreeing claims.

1.2 Line slips

A "line slip" is an agreement where an insurer delegates its authority to enter into contracts of insurance to be underwritten by the insurer to another insurer authorised company in respect of

business introduced by a broker named in the agreement. It should not give any delegated authority to the broker and should take the form of a market reform line slip.

A line slip will usually apply to specific types of business. Once the authorised insurer has entered into a contract of insurance with the insured, the evidence of the insurance will normally be issued by means of a MRC (Market Reform Contract) line slip declaration. The line slip may also allow the authorised insurer to agree claims.

Authorised insurers do not necessarily need approval to operate a line slip (this is covered under the Market Reform Contract). However, if any delegation of authority is given to the broker, approval may be required under a delegated authority arrangement in accordance with the firm's own standard practice.

Types of Line slip

Line slips are written on either a "non-bulking" or a "bulking" basis and the differences are important in terms of the method of processing. In both instances every risk is agreed by the agreement parties.

Bulking line slips

Under this type of arrangement:

- Risks are grouped and processed via Xchanging as bulk transactions
- A Market Reform Contract (Line slip) contract is formed – see MRC (Line slip) Implementation Guide, February 2018
- This includes a Unique Market Reference (UMR)
- The broker prepares bordereau in accordance with the line slip terms and conditions
- Premium bordereau intervals will be specified
- Insurer contract documentation may either be a copy of the MRC slip or an insurance policy (latter will be signed by Xchanging Ins-sure Services (XIS) or underwriters)

Non-bulking line slips

Under this type of arrangement:

- Individual risks are processed separately by the broker, as if they were "open market"
- The Market Reform Line slip is used – declarations off line slips follow the Market Reform Contract Open Market (September 2018) Implementation Guide
- The MRC (Line slip Declarations) Implementation Guide provides further information
- The UMR and Lloyd's Policy Signing Office (LPSO) Signing Number and Date for the line slip must be clearly shown on the declarations off the line slip
- A declaration off the line slip should not contain Open Market lines unless expressly permitted by the line slip
- No bordereau are normally produced
- Premium payment terms are specified for each declaration

MRC guidelines can be found on the London Market Group website at https://www.londonmarketgroup.co.uk.

Management of Line slips – Oversight Standards by the Insurer

It is recommended that each line slip written should be reviewed and authorised by the appropriate personnel within the insurer prior to inception and renewal and for the facility to be monitored carefully thereafter.

We recommend that firms include line slip business in their internal audit processes and performance reporting.

Follow markets – information levels

Follow markets on non-bulking line slips should receive information regarding risks bound as per the clauses within the line slip contract. This matter is addressed later in the Guidance for Delegated Authorities (see Table 5.2 B). We would expect follow markets to ensure that the contract is set up to provide them with all necessary information, including reports, suitably quantified in an appropriate way for the class of business concerned.

1.3 Consortium arrangements

A Consortium is a contractual arrangement under which one or more insurers delegate(s) authority to another insurer (the "Consortium Leader") to enter into contracts of insurance on their behalf. A Consortium will underwrite and bind specified classes of business produced from more than one broker (which is the main difference to a line slip).

In setting up such an arrangement a written agreement should be drawn up between the participating underwriters (the Consortium Agreement). This agreement will specify the terms under which the Consortium will operate, in addition to those terms that should be included in outsourcing agreements (see Section 5).

1.4 The legal position of the parties involved in an arrangement to delegate authority

It is important to understand all relevant parties' legal obligations in an arrangement to delegate insurer authority. The following section provides a summary overview under English law. However, the relationship between the relevant parties will depend on the individual circumstances of the contract of delegation and the parties should ensure they seek their own legal advice where required.

If an insurer delegates authority to a Coverholder, the general principle is that the Coverholder acts on behalf of the insurer and is not the policyholder's agent for the purposes of arranging the insurance. The Coverholder is therefore contracting on behalf of the firm when binding risks and issuing contractual document.

The Coverholder may also act as an agent to collect premiums, settle complaints or handle claims. The Coverholder's authority will be set out in the binding authority agreement entered into with the insurer firm.

When a broker acts as a Coverholder there is a potential conflict of interest between the broker's duties to that insurer and to policyholders in circumstances where the broker has also been appointed by the policyholders to obtain insurance. In such circumstances, it is vital for the insurer to make sure the broker manages this conflict of interest properly.

1.5 Other arrangements which may raise "delegated authority" issues

There are two other types of contract an insurer may enter into with third parties which have some of the features of delegated authority, but which are generally not treated as Coverholder arrangements; marine open cargo covers and master/group policies. In addition, there may be issues as to whether the selling of insurance policies over the internet may involve delegated authority.

1.5.1 Marine Open Cargo Covers

A marine open cargo cover is an arrangement under which an insurer provides the insured with a general grant of marine cargo insurance relevant to their business activities. (The Marine Insurance Act 1906 refers to the term "assured". However, the term "insured" is used throughout this section and has the same meaning.) That insurance covers the insured's own property, or property which the insured has had, or is expected to gain, an insurable interest in. (An insurable interest is defined as

an interest which, under the law of England and Wales, would exist if the insured were domiciled or present in England or Wales.) Typically, the insured makes separate declarations under the marine open cargo cover during the year, using agreed rates, terms and conditions.

The term marine cargo open cover includes insurance contracts issued to freight forwarders, shipping agents, carriers or other parties acting on behalf of their principals or as bailees. (A bailee is the party the insured has entrusted the goods to and has instructed to arrange marine cargo insurance.)

If an insurer grants a marine open cargo cover, it must make sure it knows about and complies with local licensing and regulatory requirements. The insured does not need approval from the insurer to operate a marine open cargo cover as defined above. To avoid any doubt, if the arrangement is not for the insured's own property, or property in which the insured has had, or is expected to gain, an insurable interest, this type of arrangement could be viewed as a binding authority.

1.5.2 Master/Group Policies and Schemes

The FCA define a Group Policy as:

'a non-investment insurance contract which a person enters into as legal holder of the policy on his own behalf and for other persons who are or will become policyholders and:

a) those other persons are or become policyholders by virtue of a common employment, occupation or activity which has arisen independently of the contract of insurance;

b) the common employment, occupation or activity is not brought about, in relation to the contract of insurance, by

    i. the insurance undertaking which effects it or carries it out; or

    ii. any activity which if carried on by a firm would be an insurance mediation activity; and

c) the risks insured under the policy are related to the common employment, occupation or activity of the policyholders.'

A master/group policy or scheme can be utilised as a way of providing coverage to individuals who belong to a group or association without the need to issue separate policies to each of the individuals. These types of arrangements have features that could constitute a form of delegated authority and insurers should give consideration as to whether this is the case and whether it may be more appropriate to write the scheme under a delegated authority agreement.

Insurer(s) should take particular care as to whether the activities of the policyholder in administering the master/group policy constitute regulated intermediary activity in the relevant territories. If the activities of the policyholder could constitute a regulated activity, the insurer should ensure that the policyholder has the necessary regulatory authorisations. Whether the policyholder is carrying on regulated activities will depend on the rules of the local territory and the activities that the policyholder will be required to perform to administer the master/group policy. In the UK, PERG 5.4 (the business test) is relevant to establish whether an unauthorised person is conducting regulated insurance mediation activity.

Lloyd's have specific guidance on Master Policies & Group Schemes which firms will need to consider if they are involved with Lloyd's business.

1.6 Electronic trading and/or Internet Selling

Insurance policies can be sold over the internet direct to policyholders. These risks will often be bound online and the policy may either be issued directly from the website on placement or will be sent after the risk has been bound. There are also electronic trading systems which allow brokers and underwriters to trade in a virtual environment.

Because third party providers are often involved in providing the electronic trading facility and the insurance contracts may be bound online, issues of delegation and sub-delegation can arise. Firms who are planning to sell insurance through the internet therefore need to consider the points below. This section also gives some guidance on certain cases which typically arise in this area.

Issues of delegation typically arise where the insurer appoints a third party internet based business to sell an insurer's policies online. Where the third party can bind the insurance online or where it is authorised to issue the certificates on behalf of the insurer, then the third party company should be approved as a Coverholder. For these purposes, it is irrelevant whether the third party has any underwriting discretion or that the process of selling policies and issuing certificates is wholly automated. That the insurer has the ability to log on to the third party provider's systems to change or stop the underwriting is also irrelevant. If policies can be bound through the online facility or certificates can be issued on the systems of the third party provider, this could be considered delegated authority and should comply with the firm's internal requirements.

Where the business is already being written through a Coverholder and the Coverholder wishes to sell policies through a third party website, in a similar manner to that described above, issues of sub-delegation can arise. In these cases, a tri-partite Coverholder arrangement may be appropriate. Because the internet is borderless, difficult licensing questions can also arise where individuals from different jurisdictions look to buy policies from the online platform. It will therefore be important for firms to check the way in which the platform can be accessed by customers, to ensure that policies are always only sold in accordance with the firm's own licences and regulatory authorisations. Where appropriate, controls should be included to ensure policies can only be sold to customers in the target risk location.

Note that in general, no issues of delegation arise in the case of "aggregator" sites. Generally, these sites allow prospective policyholders to input basic placing information and the site then provides a list of relevant policies that can be obtained. However, the "aggregator" site will not itself bind the risk but will "bounce" visitors to the website of the selected insurer for binding. Therefore the aggregator site is not carrying out any delegated authority, the policy will be bound on the firm's or Coverholder's own site. However, if the "aggregator" site does bind the policy or issue certificates, even if it uses rates and terms provided by the insurer, then there is delegated authority and Coverholder approval is required as set out above.

More difficult cases can arise where the third party site is merely providing an interface (perhaps for branding purposes) or an IT outsource solution for the operating of the insurer's or Coverholder's online binding facility. Generally, it is the firm who has physical control of the IT system that is responsible for binding the risk. If the third party is merely providing a branded front for the insurer/Coverholder's own systems, which are under the control of the insurer/Coverholder, then it is unlikely that the third party will need Coverholder approval. Where the third party has control over the system, then Coverholder approval may be required and a formal contract should be agreed.

Certain providers also now operate systems which act as trading platforms between underwriters and brokers. On these systems the third party merely acts as an IT "utility" for the parties, who will see themselves as dealing with their counterpart insurer/broker rather than with the third party provider. The arrangement in this case is similar to where the parties deal by telephone or email, where the telephone /email merely acts as a facility for the brokers and underwriters to communicate. In these cases, it is unlikely that Coverholder approval will be required.

SECTION 2 - DELEGATED AUTHORITY STANDARDS

2.1 Regulatory Requirements

The regulators rules and Financial Services and Markets Act 2000 (FSMA), supplemented by guidance, set out the extent of the obligations to which firms entering into delegated authority arrangements are subjected. The following is not intended as an exhaustive summary but describes the more relevant provisions at the time of publication.

In addition to the summaries below, applicable rules have been considered throughout the guidance.

A Note on Brexit: The United Kingdom officially left the European Union (EU) on the 31 January 2020 and is no longer directly subject to EU rules and regulations. That being noted, pre-existing EU and EIOPA rules and guidance have continued relevance as they concern measures transposed and implemented in the UK before this deadline. As such, references may be made in this guide to relevant EU and EIOPA texts. Firms should remain conscious of future divergence.

Threshold Conditions (COND)

All firms are subject to the regulatory Threshold Conditions. For firms whose business model includes outsourcing, and/or who enter into arrangements with another firm that acts to provide products or services, the following Threshold Conditions may be particularly relevant:

- Suitability
- Business model
- Appropriate resources

Principles for Businesses (PRIN)

The FCA Principles for Businesses are obligations that all authorised firms must comply with. The following Principles are particularly relevant in identifying the responsibilities of firms in relation to the regulated activities they undertake, where multiple firms are involved in providing insurance products. This includes where they are outsourcing these activities or performing these activities under an outsourcing arrangement:

- Principle 2 - ‘A firm must conduct its business with due skill, care and diligence’.
- Principle 3 - ‘A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems’.
- Principle 6 - ‘A firm must pay due regard to the interests of its customers and treat them fairly’.
- Principle 7 'A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading'.
- Principle 8 - ‘A firm must manage conflicts of interest fairly, both between itself and its customers and between a customer and another client’.

Principle 6 sits behind many of the FCA’s detailed rules and they expect customers’ interests to be at the heart of how firms do business.

Senior Management Arrangements, Systems and Controls (SYSC)

SYSC contains rules and guidance to amplify Principle 3, relating to operational risk (including the risk that firms do not meet the FCA’s Principle 6 expectations with regard to treating their customers fairly) including outsourcing.

SYSC requires that a firm must take reasonable care to establish and maintain such systems and controls that are appropriate to its business. Guidance set out in SYSC indicates that the complexity and diversity of its business should be relevant factors to be considered by a firm, and that firms should carry out regular reviews to ensure ongoing appropriateness. SYSC also requires firms to

identify and manage their conflicts of interest.

SYSC includes knowledge and ability requirements that apply to the distribution of insurance, which may apply to Coverholders when undertaking outsourced activities. In addition, SYSC 19F.2 prohibits remuneration and performance management practices that would conflict with the customer's best interests rule (see following section on ICOBS).

SYSC 19F.2 states as follows:

(1) Insurance distributors must not:

a) be remunerated; or

b) remunerate or assess the performance of their employees,

in a way that conflicts with their duty to comply with the customer's best interests rules.

(2) In particular, an insurance distributor 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 the insurance distributor could offer a different insurance contract which would better meet the customer's needs.

One of the key issues that a firm is expected to consider in establishing and maintaining the systems and controls appropriate to its business, as required by the FCA rules, relates to situations where a firm's governing body delegates to a third party and thereby outsources functions or tasks for the purpose of carrying out its business.

Functions typically outsourced by insurers include:

- Underwriting
- Claims management
- Complaint handling

Firms should take reasonable care to supervise the discharge of outsourced functions by the third party. A firm cannot contract out of its regulatory obligations, and appropriate safeguards should be put in place, including the following:

- A firm should assess whether the recipient is suitable to carry out the delegated function or task, taking into account the degree of responsibility involved.
- The extent and limits of any delegation should be made clear to those concerned.
- There should be arrangements to supervise delegation, and to monitor the discharge of delegates' functions or tasks.
- To ensure that by outsourcing functions, senior personnel do not delegate their responsibility.
- If cause for concern arises through supervision and monitoring or otherwise, there should be appropriate follow-up action at an appropriate level of seniority within the firm.
- A firm should take steps to obtain sufficient information from its delegate to enable it to assess the impact of delegation on its systems and controls.

SYSC also applied to incoming EEA firms in relation to activities carried on from an establishment in the UK and will still apply to those firms that are operating under the Temporary Permissions Regime while awaiting full UK authorisation.

Insurance: Conduct of Business sourcebook (ICOBS)

ICOBS outlines high-level standards that apply to all non-investment insurance product sales (general insurance and protection policies). ICOBS also states that firms must take reasonable steps to give their customers appropriate information about a policy in good time and in a comprehensible way so they can make an informed decision. This applies before and after the product is bought. The information given will depend on the customer, the policy's terms and its complexity. In addition, any

advice given must be suitable for the customers.

The Insurance Distribution Directive (IDD) came into force on the 1st October 2018 and was incorporated into the FCA rules, including ICOBs. The IDD introduced the 'customer's best interests' rule, which has been incorporated into ICOBS 2.1: A firm must act honestly, fairly and professionally in accordance with the best interests of its client. The IDD also introduced requirements regarding the cross-selling of products, including optional extras. These requirements have been incorporated into ICOBS 6A.

The FCA have indicated that the introduction of the IDD represents a material change in terms of what is required in respect of the oversight of insurance distribution, which may necessitate a review of a firms' risk appetite with regard to their delegated authority strategy and operations.

ICOBS 8 sets out the regulatory requirements applicable to insurers in relation to claims handling. ICOBS 8.1.1R states that 'an insurer must handle claims promptly and fairly; provide reasonable guidance to help a policyholder make a claim and appropriate information on its progress; not unreasonably reject a claim (including by terminating or avoiding a policy); and settle claims promptly once settlement terms are agreed'. Insurers who outsource claims handling therefore need to ensure that they do so with appropriate care and diligence so that they are able to continue to satisfy this regulatory responsibility and ensure that customers receive fair outcomes. It is expected that regardless of the length of any particular distribution chain, any claims service should not suffer detriment due to the length of that chain.

Product Intervention and Product and Governance Sourcebook

The FCA have incorporated Insurance Distribution Directive (IDD) product oversight and governance rules into UK regulation and the full product rules can be found in FCA Handbook under PROD 4. In addition to the FCA rules, the European Insurance and Occupational Pensions Authority (EIOPA) issued guidelines on this topic, as summarised below:

- Insurance undertakings, as well as intermediaries which manufacture any insurance product for sale to customers, shall maintain, operate and review a process for the approval of each insurance product, or significant adaptations of an existing insurance product, before it is marketed or distributed to customers.
- The product approval process shall be proportionate and appropriate to the nature of the insurance product.
- The product approval process shall specify an identified target market of customers for each product and ensure that all relevant risks to such identified target market are assessed, the intended distribution strategy is consistent with the identified target market and take reasonable steps to ensure that the insurance product is distributed to the identified target market.
- The insurance undertaking shall understand and regularly review the insurance products it offers or markets, taking into account any event that could materially affect the potential risk to the identified target market, to assess at least whether the product remains consistent with the needs of the identified target market and whether the intended distribution strategy remains appropriate.
- Insurance undertakings, as well as intermediaries which manufacture insurance products, shall make available to any distributor all appropriate information on the insurance product and the product approval process, including the identified target market of the insurance product.
- Where an insurance distributor advices on or proposes insurance products which it does not manufacture, it shall have in place adequate arrangements to obtain the information referred to in the fifth subparagraph and to understand the characteristics and identified target market of each insurance product.

The FCA provided additional guidance for product manufacturers in PS18/1 on implementing the IDD into UK regulation as follows:

- The guidance that manufacturer firms should make sure distributors have the necessary knowledge, experience or competence to understand the product and the target market isn't intended to stop manufacturers selecting distributors who don't have experience with a particular product. Instead, the manufacturer should consider what knowledge, competence or training is needed by distributors in order to meet the guidance.
- Where a distributor firm is regarded as a 'co-manufacturer' for the product governance rules, they must still follow the other rules for distributors, including the distributor product governance rules.
- Where an intermediary is regarded as a 'co-manufacturer' for the purposes of the product governance rules, they will need to ensure that the product review process takes appropriate account of any direct distribution they undertake. Firms that distribute products they manufacture may wish to consider the distributor product governance rules to assess whether the product remains consistent with the needs of the identified target market and whether the intended distribution strategy remains appropriate. Firms that both manufacture and distribute their own products will need to consider other FCA rules relevant for distributors including, for example, those relating to systems and controls in SYSC or conduct requirements in COBS or the Insurance Conduct of Business Sourcebook (ICOBS).
- When a manufacturer is carrying out a review of a product, they should consider what information is needed and which other firms in the distribution chain to approach to ask for it. Where the distribution chain is long, we would still expect manufacturers to be able to find out which firms distribute their products if they need the information. For example, if they need additional data that can't be supplied by the firms with which they deal directly, they could ask those firms to gather it.

The Responsibilities of Providers and Distributors for the Fair Treatment of Customers (RPPD)

RPPD is a Regulatory Guide that develops Principles 2, 3, 6 and 7 (see PRIN) and sets out the FCA's view on what the combination of the Principles and detailed rules, mean to both providers and distributors, who supply products or services, in order to ensure customers are treated fairly. It applies to both insurers and insurance intermediaries.

The FCA state that customer's experience should not be affected by whether a product or service was provided and distributed by a single institution or by two or more institutions.

Providers and distributors should consider the impact of their action (or inaction) on the customer in various stages of the product life-cycle, or the various stages of provision of the service. Depending on the precise nature of a firm's business, this could mean addressing the fair treatment of customers at the following stages: design and governance; identifying target markets; marketing and promotion; sales and advice processes; after-sales information and service; and complaints handling.

RPPD uses the terms 'provider' and 'distributor' but recognises that responsibilities flow from 'the actual roles or functions undertaken in a transaction. Firms should take this into account in considering their responsibilities under the Principles. In considering which responsibilities apply to it, a firm should consider the functions and roles that it undertakes in the product life-cycle. Whether a particular role or function is fulfilled by the distributor or provider (or both), may vary based on the product or service and particular arrangements in place. It may be possible for a firm to act as both provider and distributor at the same time in respect of different products or services.

It follows that the status of a firm, whether insurer or insurance intermediary, does not determine whether such firm should be considered to be a 'provider' or a 'distributor' for the purposes of identifying relevant responsibilities. Instead the RPPD is clear that firms need to consider exactly what functions they are performing, in relation to any given product/transaction, in order to establish which responsibilities it has. The RPPD states that whether firms can agree to apportion responsibilities between themselves will depend on the circumstances, which will include:

- The nature of the regulatory responsibility.

- The extent to which such an agreement would be reasonable.
- Whether the arrangement is clear to both parties and properly recorded.
- The systems and controls used to monitor whether the agreement continues to be appropriate in the circumstances.

By way of example, the RPPD states that where an insurer is commissioned by a distributor to create a product, where the criteria for the product are specified by the distributor, many of the responsibilities fall to the commissioning distributor as 'retail manufacturer' of the product rather than the 'pure manufacturer' of the commissioned product or service. However, the pure manufacturer must still act in accordance with relevant Principles applicable to its functions, including for example acting with due skill, care and diligence in accordance with Principle 2.

It goes on to address respective provider and distributor responsibilities, and to set out guidance as to how such responsibilities may be met.

Provider responsibilities

The provider responsibilities, which may, depending on the facts, be carried out by insurance intermediaries as retail manufacturers rather than insurers as pure manufacturers, are:

- Product design
- Provision of information to distributors
- Provision of information to customers
- Selection and appropriateness of parties and distribution channels
- Post-sale responsibility (including claims and complaints)

Providers should also consider whether the sale of the product should be advised or non-advised and whether the product can be sold online, via telephone sales or face to face. Providers should have a clear approach to the management of the distribution chain and be able to exercise significant control over the distribution network. Providers are expected to review whether what is happening in practice is consistent with their plans and expectations for the distribution of the product.

Distributor responsibilities

Distributor responsibilities, which may be assumed by insurers as well as carried out by insurance intermediaries, are:

- Financial promotions
- Provision of information to a customer before the point of sale
- Advising on selection of provider
- Post-sale responsibility

Solvency II Directive (2009/138/EC)

Under the Solvency II Directive, Article 49 addresses outsourcing and details firms' responsibilities as follows:

1. Member States shall ensure that insurance and reinsurance undertakings remain fully responsible for discharging all of their obligations under this Directive when they outsource functions or any insurance or reinsurance activities.

2. Outsourcing of critical or important operational functions or activities shall not be undertaken in such a way as to lead to any of the following:

    a) materially impairing the quality of the system of governance of the undertaking concerned
    b) unduly increasing the operational risk
    c) impairing the ability of the supervisory authorities to monitor the compliance of the undertaking with its obligations
    d) undermining continuous and satisfactory service to policy holders

3. Insurance and reinsurance undertakings shall, in a timely manner, notify the supervisory authorities prior to the outsourcing of critical or important functions or activities as well as of any subsequent material developments with respect to those functions or activities.

While the UK is undertaking a review of Solvency II, it is not expected that the rules on outsourcing or firms' responsibilities will change.

PRA Expectations and EIOPA Guidelines on Systems of Governance

EIOPA have issued to National Competent Authorities guidelines in respect of Solvency II. In 2015, EIOPA issued Guidelines on Systems of Governance, which includes guidelines that relate to outsourcing requirements. The PRA expects firms to comply with all of the System of Governance Guidelines that apply to them, in a proportionate manner. The EIOPA guidelines on outsourcing read as follows:

Section 11: Outsourcing

Guideline 60 - Critical or important operational functions and activities

The undertaking should determine and document whether the outsourced function or activity is a critical or important function or activity on the basis of whether this function or activity is essential to the operation of the undertaking as it would be unable to deliver its services to policyholders without the function or activity.

Guideline 61 - Underwriting

When an insurance intermediary, who is not an employee of the undertaking, is given authority to underwrite business or settle claims in the name and on account of an undertaking, the undertaking should ensure that the activity of this intermediary is subject to the outsourcing requirements.

Guideline 62 - Intragroup outsourcing

If critical or important functions or activities are outsourced within the group, the participating insurance or reinsurance undertaking, the insurance holding company or the mixed financial holding company should document which functions relate to which legal entity and ensure that the performance of the critical or important functions or activities concerned at the level of the undertaking is not impaired by such arrangements.

Guideline 63 - Outsourcing written policy

The undertaking that outsources or considers outsourcing should cover in its policy the undertaking's approach and processes for outsourcing from the inception to the end of the contract. This in particular should include:

a) the process for determining whether a function or activity is critical or important;

b) how a service provider of suitable quality is selected and how and how often its performance and results are assessed;

c) the details to be included in the written agreement with the service provider taking into consideration the requirements laid down in Commission Delegated Regulation 2015/35;

d) business contingency plans, including exit strategies for outsourced critical or important functions or activities.

Guideline 64 - Written notification to the supervisory authority

In its written notification to the supervisory authority of any outsourcing of critical or important functions or activities, the undertaking should include a description of the scope and the rationale for the outsourcing and the service provider's name. When outsourcing concerns a key function, the information should also include the name of the person in charge of the outsourced function or

activities at the service provider.

The rules on outsourcing in the PRA rulebook can be found under the section entitled: Conditions Governing Business 7 – Outsourcing. These read as follows:

7.1 If a firm outsources a function or any insurance or reinsurance activity, it remains fully responsible for discharging all of its obligations under the rules and other laws, regulations and administrative provisions adopted in accordance with the Solvency II Directive.

7.2 A firm must not outsource a critical or important operational function or activity in such a way as to lead to any of the following:

1) materially impairing the quality of the firm's system of governance;
2) unduly increasing the operational risk;
3) impairing the ability of the supervisory authorities to monitor the firm's compliance with its obligations;
4) undermining continuous and satisfactory service to policyholders.

7.3 A firm must, in a timely manner, notify the PRA prior to the outsourcing of critical or important functions or activities as well as of any subsequent material developments with respect to those functions or activities.

7.4 Without prejudice to 7.1 to 7.3, a firm outsourcing a function or an insurance or reinsurance activity must take the necessary steps to ensure that the following conditions are satisfied:

1) the service provider must co-operate with the PRA and, where relevant, any other supervisory authority of the firm in connection with the function or activity that is the subject of the outsourcing;
2) the firm, its auditors, the PRA and, where relevant, any other supervisory authority of the firm must have effective access to data related to the functions or activities that are the subject of the outsourcing; and
3) the PRA and, where relevant, any other supervisory authority of the firm must have effective access to the business premises of the service provider and must be able to exercise those rights of access.

EIOPA Framework for Assessing Conduct Risk Through the Product Lifecycle

In February 2019, EIOPA published their framework for the assessment of conduct risk. In the report, available here, EIOPA states:

EIOPA places particular emphasis on an effective and efficient conduct of business supervision that is risk-based, pre-emptive and proactive, so as to tackle consumer detriment issues at an early stage, rather than only reacting following the emergence of problems. These objectives are at the heart of EIOPA's overarching framework for conduct of business supervision.

The purpose of the framework is to identify drivers of conduct risk and the implications of these in the emergence of consumer detriment. The framework focuses on conduct risk throughout all stages of the product lifecycle.

FCA Expectations

In June 2015, the FCA published a report which set out their findings from their thematic review of delegated authority; TR15/7 Delegated Authority: Outsourcing in the General Insurance Market. The regulator shared the findings with the industry so that firms could consider to what extent they were impacted by the issues found and what changes they needed to make to ensure that their customers were treated fairly.

In the report, the FCA set out their expectations, in particular:

- Insurers delegating underwriting or other authority to external parties to recognise that they are outsourcing and to consider whether they have effective and risk-based controls (which appropriately consider conduct risks) in place. These controls should address both the initial decision to outsource and the ongoing monitoring of the performance of the outsourced function and resultant product(s). Insurers should take steps to address any gaps they identify in the control framework and should review their existing outsourcing relationships to identify and remediate any shortcomings in the operation of these arrangements.
- Insurers to assess whether the claims handling approach and processes in place where they have outsourced claims handling are appropriate and will ensure that claims are handled promptly and fairly. This assessment should include the consideration of whether any potential conflicts of interest arising from incentive arrangements are appropriately mitigated. Where they identify deficiencies they should ensure that these are addressed.
- Insurers to consider forthcoming changes to governance requirements for firms arising from Solvency II to assess how these impact their activities, particularly in relation to outsourcing, and to assess what actions they need to take to ensure that they are able to comply with these requirements.
- Insurers and intermediaries to consider the extent to which each may be performing the functions of a 'product provider' and to clearly identify what responsibilities flow from that for each including for product design and the ongoing monitoring of the performance of the insurance product for customers. To the extent that the circumstances and regulatory responsibilities allow firms to agree the apportionment of responsibilities, this should be reasonable and clear to both parties.
- Insurers and intermediaries to review their existing monitoring activity and MI in relation to outsourced arrangements and allocated functions to assess whether this is appropriate and allows them to identify poor customer outcomes and instances where customers are not being treated fairly. Firms should also consider whether this information is reviewed appropriately, shared as necessary and acted upon. Where gaps and shortcomings are identified these should be addressed.
- Insurers and intermediaries acting as 'product provider' to assess the appropriateness of the existing distribution channel and sales activities, the efficacy of the arrangements and processes in place to mitigate the risks to customers posed by the distribution channel and the adequacy of the ongoing oversight and monitoring of the distribution chain (including the MI used to facilitate this). Any gaps or shortcomings identified should be addressed.
- Insurers and intermediaries should note that the recast Insurance Mediation Directive, which is currently under negotiation, will include measures relating to product oversight and governance. Additionally, EIOPA consulted on product oversight and governance guidelines in relation to insurance undertakings manufacturing insurance products. These have the potential to strengthen the requirements placed on firms that manufacture insurance products and the FCA expects firms to ensure that their practices are adjusted to meet any new requirements.

It should be noted that the FCA consider (re)insurers to be the product manufacturers, or at the very least, co-manufacturers if another entity is involved in the manufacture process. Firms are not able to outsource all product manufacturer responsibilities.

Where these expectations are based on the regulators existing Handbook requirements, the FCA expect firms who identify shortcomings when undertaking any assessment to act promptly to remediate these issues.

In the 2019 General Insurance Distribution Chain thematic review, the FCA set out its findings on two pieces of work, a thematic review of Value in the GI Distribution Chain and a multi-firm review of delegated authority arrangements. The report identified significant potential for harm and poor outcomes for customers, arising from the product development and distribution approaches in some sectors of the GI market. These harms include, for example, customers purchasing products that are not appropriate for them or customers paying increased prices due to remuneration paid to firms in

the distribution chain who incur little cost or deliver little benefit. The regulator states that these potential harms are caused by firms not adequately considering the value of the products or services provided to customers, as well as failures in product design, weak oversight of the distribution chain, poorly designed distribution strategies and conflicts of interest caused by firms' remuneration structures.

It was emphasised that many GI firms had not responded appropriately to the FCA's 2015 findings and expectations and that they were not sufficiently focussed on customer outcomes, including the value of the products and services provided. The FCA stressed that they will not hesitate to take further action if they encounter issues and potential failings at firms that cause harm or have potential to cause harm to customers.

Much of the 2019 thematic review findings were focussed on the value and final price of the product that was sold to the customer, which included fees and commission charged by the entities in the distribution chain. Some of the key points are as follows:

- Manufacturers should consider the total price (including all fees and commission charged by all entities in the chain) the customer will pay. Where a net rate has been offered to another party in the chain, the manufacturer should be aware of the final selling price.
- Manufacturers must ensure that the final selling price of a product bears a reasonable relationship with the risk premium and the benefits or services provided to the customer.
- Manufacturers should also clearly understand the benefits provided to the customer by the involvement of each party in the distribution chain and how this reasonably relates to their remuneration.
- If a manufacturer delegates activities to other parties within the distribution chain, **including to firms who are not regulated**, they must have adequate systems and controls to ensure that these activities are delivered in line with the manufacturer's obligations.

Where a firm concludes that a remuneration arrangement conflicts with their duty to act in accordance with the customers best interests rule, the regulator expects firms to amend the arrangement. Unlike other situations which give rise to potential conflicts of interest identified in relation to insurance distribution activities (such as conflicts of interest covered by SYSC 10), disclosure cannot be relied on as a satisfactory means of managing the conflict or as a measure of last resort in this area.

Conduct Risk

The FCA in their Risk Outlook 2013 describe conduct risk as inherent factors, structures, behaviours and environmental factors that are present in the financial sector and how they impact the financial services market, its participants and particularly the interests of its customers. The FCA continue to focus on how firms are managed and structured to ensure consumers are at the centre of their business, pay due regard to the interests of their customers and treat them fairly at all times. As mentioned earlier in this section, EIOPA have published a framework for the assessment of conduct risk throughout the product lifecycle and firms may wish to consider the guide in full.

Firms are expected to ensure that they are putting customers and the integrity of markets at the heart of their business models and strategies. This includes making strategic cultural changes which promote good conduct, establishing oversight around the design and innovation of products and services and ensuring they are transparent in their dealings with customers. This is of particular importance when delegating authority to a third party. Most importantly, firms must take an active role in maintaining the integrity of the financial markets to ensure customers can have confidence in the firms and products they engage with.

It is expected that all insurers will identify, assess and manage conduct risk to ensure fair outcomes are achieved for all customers, and be able to evidence that they have done so.

Firms will need to give particular consideration to the procedures in place to address the conduct risk posed by delegated authority. These procedures should include at a minimum:

- How conduct risk should be assessed for a binding authority.
- Conduct related due diligence requirements and how this should be evidenced.
- Ongoing monitoring requirements for conduct risk.

These procedures may form part of a firms delegated authority procedures or their overarching conduct procedures as appropriate, provided conduct risk in delegated authority is appropriately addressed.

Conduct Risk - Client Considerations

Firms will need to give particular consideration in cases where the end purchaser can be considered a consumer or a less sophisticated customer.

Binding authorities that include products that will be sold to consumers and less sophisticated customers are therefore likely to pose the greatest conduct risk. It is important that this conduct risk is carefully assessed and managed and that this is evidenced, including the documentation of the reasons the firm is satisfied that customers will receive fair outcomes.

The FCA describes a consumer as any natural person acting wholly or mainly for purposes outside their trade, business or profession, in contrast to business clients who are acting wholly and mainly/predominantly for the purposes of their trade, business or profession. It should be noted, however, that the term 'consumer' has different meanings under different pieces of legislation and the FCA has stated there is no strict rule to designate a consumer.

The FCA has suggested that Micro-enterprises should be afforded the same treatment as consumers. A Micro-enterprise is deemed an enterprise which:

- Employs fewer than 10 persons and
- has a turnover or annual balance that does not exceed €2 million

The FCA has further noted that some segments of the SME population may also have a need for extra consideration. This would include, but is not limited to:

- Small and simple businesses buying products and services in which they do not have significant expertise should generally have the greatest access to consumer provisions.
- Larger SME's with sophisticated operations have less need for such provisions, except when making purchases unrelated to their core business, without relevant expertise.

Consideration should be given to any other entity that would be considered a consumer by the relevant regulatory authority in the local territory.

Firms will also need to consider products that have been previously considered as wholly commercial; in particular, where these are sold to an individual or small business, e.g. aviation or marine policies.

Firms may wish to examine the following areas when considering clients:

- Product design and suitability
- Financial Promotions
- Product distribution, including methods and information
- Barriers to customers
- Claims responsibility and barriers to the claim process
- Complaints responsibility
- Renewal transparency responsibility
- Fair treatment of customers
- Reporting requirements
- Compliance with international conduct requirements (where applicable)

Competition and Market Share

Insurers must give consideration to competition law and market share matters, including any relevant regulation. The FCA have powers to enforce UK competition law regarding the provision of financial services. These competition powers may also be used by the Competition and Markets Authority (CMA) in all sectors of the economy, including financial services. This means that for financial services the CMA and the FCA have 'concurrent powers' and the FCA is a 'concurrent regulator'.

Competition law forbids:

- cartels and other potentially anti-competitive agreements, and
- abuse of a dominant position

Examples of cartels include agreements to fix prices or share markets. Examples of other potentially anti-competitive agreements include a distributor agreeing with its supplier not to sell below a particular price.

Examples of abuse of a dominant position include a dominant business charging prices so low they do not cover the costs of the product or service sold, with the aim of driving out competitors and then increasing prices again. Or, refusing to supply an existing or long-standing customer without objective justification.

Further, the European Commission decided that in its opinion, there were no valid reasons for the continuation of the Insurance Block Exemption Regulation and has decided that it would lapse on 31 March 2017. Insurers are therefore no longer able to rely on any of the provisions that were contained therein and will need to assess their co-operation in the market context to see whether it is in line with competition law and antitrust rules. This position is unchanged for UK entities following Brexit.

Subscription

Where binding authorities are written on a subscription basis, it is likely that the primary obligation will be on the lead insurer. Although all of the participating insurers will need to ensure that they have a written strategy for entering into such an agreement and effective systems and controls have been implemented and are met. In particular, it is likely that the lead insurer will have the main responsibility for assessing the Coverholder, setting up the contract of delegation, setting any limits on the Coverholder's authority and primary monitoring of the contract of delegation. Throughout this guidance, these insurers are referred to as 'the lead insurer'.

Following insurers are expected to have a written strategy and roadmap set out internally that articulates clearly why any follow arrangement is entered into, be satisfied that the lead insurer conducts appropriate due diligence and has at least the same standard of systems and controls as the follow insurer would implement themselves. Follow insurers should regularly obtain/receive evidence to enable performance of ongoing monitoring of all Coverholders with whom they have a relationship in line with their delegated authority strategy, paying particular attention to claims and complaints handling..

Where a firm adopts the lead insurer position, it should ensure that all relevant due diligence information and monitoring data is available and shared on a regular basis with the following market.

SECTION 3 - A STRATEGY FOR DELEGATED AUTHORITY

3.1 Introduction

It is expected that firms will have a clear risk appetite for entering into and managing delegated underwriting contracts that is articulated through written policy and procedures and agreed at Board level. The risk appetite should have regard to not only prudential matters, but should consider operational and conduct issues and how the strategy fits with the wider corporate strategy. The policy and procedures should be applied consistently to all agreements managed by the insurer and regularly reviewed and updated.

The competencies needed for managing delegated underwriting arrangements are different to those needed for other methods of acceptance.

Firms will need to satisfy themselves that they have the control and resources (both systems and individuals with suitable experience and skills) to enter into and manage delegated underwriting arrangements effectively, taking into account:

- The number of Coverholders
- The number of contracts which an insurer leads or follows
- The extent or range of delegation
- The volume of income
- The classes of business
- The products being underwritten
- The conduct implications (also see Section 7)
- The operational implications
- The potential conflicts of interest
- The number of customers involved
- The customer needs
- The likely customer outcome
- The level of exposure (e.g. catastrophe exposure)
- The geographical distribution
- The method of distribution
- Capabilities of current IT/systems especially as regards bordereau management and exception reporting
- The overall number of delegated agreements the insurer undertakes

3.2 What should be included in the strategy?

The strategy needs to take account of the impact on the firm's business of the outsourcing arrangements to Coverholders, apply a risk based approach to the selection of Coverholders, consider the reporting and monitoring arrangements to be implemented, and the extent of the level of authority delegated.

As a guide, it should include the following sections:

An executive summary

An overview of what the firm's current position is on Coverholders and Binding Authorities, plus an outline of the objectives for the year ahead.

Business rationale

An explanation as to why the insurer wishes to delegate authority to Coverholders. This may include an analysis of:

- The expected gain from delegating authority to Coverholders
- Current and projected market conditions
- Territorial considerations
- How such arrangements would fit with the insurer's organisation and reporting structure; business strategy; conduct risk appetite; operational risk; overall risk profile; and ability to meet its regulatory obligations
- How such arrangements would result in appropriate customer outcomes

Roadmap

This may include information on:

- Resourcing (both systems and individuals)
- How suitable Coverholders will be identified
- The extent of delegation
- The extent and nature of distribution (including the length of the distribution chain)
- The capacity in which each link in the distribution chain is acting (including consideration of data protection responsibilities)
- The service and value each link in the distribution chain will provide
- The rationale, including due diligence, oversight and control measures for any sub-delegation granted
- The potential conflicts of interest
- The likely customer outcome
- Remuneration arrangements, both internal and external, paying particular attention to SYSC 19F.2 (profit commission and similar incentives should only be considered where there are robust controls to mitigate the conflicts of interest that they give rise to)
- Consideration of the total price the customer will pay, including fees charged by all the distributers in the chain
- How claims will be handled
- How complaints will be handled
- Performance management, both internal and external
- Cross-selling considerations
- Pre-approval due diligence
- Appropriate MI to be generated and shared with relevant parties
- An overall process framework specifying the procedures for ensuring that effective due diligence is carried out and evidenced by all involved at inception and renewal of contracts, as well as throughout the year when monitoring that reporting is in line with contract conditions
- Competition law and market share considerations
- Consideration and compliance with any applicable overseas laws & regulatory or tax requirements

It should be noted that when delegating authority, it usually entails granting 'Risk Transfer' to the chosen Coverholder (i.e. that the Coverholder is holding the money on behalf of the firm) and that firms will need to outline in their roadmap how Coverholders should hold client monies on their behalf. Whether a firm chooses to allow their Coverholders to co-mingle premiums with other insurers and/or policyholders or requires a separate segregated bank account, this should be reflected in the binding authority agreement. The FCA requirements on client money arrangements can be found in the Handbook under CASS 5.

Product Design and Underwriting

Firms must have robust product oversight and governance arrangements and should consider the

following in any product that they design, including those that will be distributed via delegated authority. It should be noted that the FCA consider (re)insurers to be product manufacturers, or at least co-manufacturers for any delegated authority arrangement. Firms should:

- Maintain, operate and review a product approval process for new products, and for existing products to which significant adaptations have been made, before such products are marketed or distributed.
- Ensure staff involved in product design and manufacture have the necessary skills, knowledge and expertise for their role.
- Specify a target market for each product, including where relevant, identifying groups of customers for whom the product is generally not compatible, including consideration of the degree of financial capability and literacy.
- Design products to be compatible with the needs, characteristics and objectives of the target market, including consideration of the quality and value of the product.
- Assess the product wording in relation to customer outcomes as well as underwriting results.
- Establish the information they will need to provide to customers, including remuneration disclosures, any required Insurance Product Information Documents (IPIDs), cross-selling information (if applicable) and any renewal transparency requirements.
- Test the product before bringing it to the market.
- Select distribution channels that are consistent with the target market, which must include an assessment of the product charging structure and the value for money the product delivers to the customer. This must also include any fees that may be charged by distributers in the chain.
- Provide all appropriate information on products and the product approval process to distributors.
- Take reasonable steps to ensure the product is distributed to the target market.
- Consider how the firm will ensure the Coverholder understands the target market and which groups of customers the product is not intended for.
- Monitor and regularly review products, to ensure the product remains consistent with the needs of the target market and that the distribution strategy remains appropriate, responding appropriately to feedback and MI.
- Appropriate transparency for the target market, ensuring manufacturers make information regarding the target market assessment undertaken available to any distributor.

Firms may also wish to consider:

- Projected Underwriting results from Delegated Authorities for the next 3-5 years including a split by:
    - Classes of business to be written
    - Geographical distribution
- Number of Delegated Authorities split by:
    - Lead Coverholder binding authority agreements (including Co-Lead)
    - Follow Coverholder binding authority agreements
    - Lead Lineslips
    - Follow Lineslips
    - Other types of delegation
- Level of catastrophe exposure

If an insurer does not write all of the binding authority, they will be responsible for placing the remainder of the contract with a following market. In these circumstances the insurer will need to be able to demonstrate that they are capable of addressing the following:

- Making sure all relevant information is given to the following market
- Keeping a record of the information given to the following market when the binding authority was placed (and keeping evidence of its agreement)
- Keeping records about the operation of the binding authority (for example, changes to the terms of cover)

- Making sure any outstanding issues are fully resolved before the binding authority comes into force
- Making sure that premiums and claims are processed to the following market

Insurer(s) should also be aware that if a broker is not involved, disputes or litigation could arise with the following market (for example, as a result of a mistake made by one of the insurer(s) staff or due to a potential misrepresentation). Firms should consider outlining all the duties, responsibilities and administration requirements in the contract in order to mitigate this risk and may also consider it appropriate to buy errors and omissions insurance to cover these risks.

In summary, therefore, the plan should reflect the strategy to be adopted when leading or when following a contract of delegation.

Products Designed by Others

Firms that are considering underwriting products designed by others will have to undertake sufficient due diligence to satisfy their obligations and responsibilities. The approach, processes and service standards should be reviewed, benchmarked and qualitatively assessed against their own internal criteria, approach and standards. This applies particularly when considering products that a firm would not otherwise underwrite. Information that should be considered, in addition to those outlined above, will include:

- The research done to create the product
- Performance of the product
- Claims frequency
- Claim declinature and repudiation rates
- Numbers of complaints
- The product wording
- The delivery of post-sales services
- The conduct risk

It is the principle view of the FCA that a customer's experience should not be affected by whether a product or service is provided and distributed by a single institution or by two or more institutions. Firms must ensure that tasks and roles are clearly allocated between the parties involved to ensure that this is achieved consistently.

SECTION 4 - DUE DILIGENCE OF COVERHOLDERS

4.1 Introduction

An appropriate level of due diligence is important not only at inception and renewal of binding authorities, but also on an ongoing basis. In order to avoid an undue burden on the parties at the time of renewal, it is recommended that the due diligence process is spread through the year.

This section highlights some of the important areas that should be considered when assessing a new Coverholder.

4.2 The internal assessment process

Firms should identify which personnel are authorised to take the final decision with regard to entering into a new Coverholder relationship or binding authority, following completion of all the procedures to assess and evidence the financial, compliance and underwriting capabilities of the Coverholder. The decision to proceed with a new Coverholder relationship or binding authority arrangement should normally be taken by a formal quorum of authorised individuals or a meeting of a delegated underwriting committee. In order to ensure that due regard is given to likely customer outcomes, firms should take a holistic operational approach to the outsourced agreement and not exclusively delegate control to one particular function, (such as underwriting). Firms must also be able to demonstrate appropriate compliance. Any internal assessment that is undertaken also needs to be appropriately evidenced and the basis of selection of a particular Coverholder should be transparent.

Firms may wish to consider the operation of a tender process in order to select a new Coverholder. The final decision will be based on factors decided by the authorised personnel with the authority to approve Coverholders and the weight attributed to each factor will depend on the outcome that the firm intends to achieve. A comparison of the elements outlined in section 4.3 should enable firms to be able to select the Coverholder most appropriate for the delegated authority.

Approval of a new Coverholder should be given via the internally approved process for the firm that is in line with the Board's underwriting strategy and risk appetite for delegated authority business. The sign off should either be cross functional or have evidence that cross functional due diligence has been carried out.

The firm's internal assessment process will involve individuals with distinct roles to play, and it should be clear who is responsible for each. Firms should clearly identify:

- The individuals responsible for introducing/identifying the Coverholder and providing the business rationale for granting a binding authority.
- The individuals responsible for initiating and controlling the due diligence process in preparation for internal approval.

Board reporting pertaining to new Coverholders should be timely and accurate and as a minimum, should be on an annual basis, although firms may wish to consider more frequent reporting taking into consideration ongoing due diligence and key staff changes.

4.3 Matters to consider when assessing a new Coverholder

Suitability Criteria

The internal review process performed by each lead insurer should aim to cover, as a minimum, the relevant suitability criteria (see table 4.3 below). In addition, the firm must be able to evidence any approval process that they have undertaken, paying particular attention to the need for a clear evidence trail demonstrating the quality and adequacy of the Coverholder.

Table 4.3

- whether the applicant is a competent, proficient and capable organisation and have regard to the following matters:

  a) the applicant's compliance with appropriate principles of good corporate governance;

  b) the quality and adequacy of the applicant's human resources, including:

     i) the competence, reputation, character and suitability of the applicant's directors, officers and staff; and
     ii) the knowledge and experience (including any minimum CDP requirements) of the applicant's directors, officers and staff regarding the conduct and regulation of insurance business, including in any other relevant jurisdiction;

  c) the quality and adequacy of the applicant's other resources, including the quality and adequacy of the applicant's:

     i) systems, procedures, protocols and arrangements for the conduct of its business;
     ii) resources to comply with appropriate service standards for its customers;
     iii) resources to comply with such principles and standards for the conduct or administration of insurance business; and
     iv) resources and systems for underwriting administration, recording and provision of management information and for the administration and agreement of claims and or complaints;

  d) the quality and adequacy of the applicant's controls and procedures to manage its business including:

     i) the applicant's arrangements for identifying, resolving or managing conflicts of interest; and
     ii) the quality and adequacy of the applicant's controls and procedures for the management of underwriting risk and for the management of the administration and agreement of claims;
     iii) the applicants arrangements for appropriate IT infrastructure, appropriate levels of data security and data protection governance, including any third–party IT services used and such facilities as cloud based services, and that it complies with any applicable data protection legislation

  e) the nature of the applicant's business including its past, present and forecast underwriting performance (including any past relationship with the firm) and the applicants targeted market;

  f) the remuneration the applicant will receive (including any fees or charges made by the applicant and/or further suppliers, to be paid by the customer) and that the chosen distribution chain provides demonstrable value to the end customer;

- whether the applicant is of appropriate reputation and standing;
- whether any person who controls the applicant or who is connected or associated with the applicant is of appropriate reputation and standing;
- whether the applicant has adequate capital and financial resources;
- whether the applicant has adequate professional indemnity insurance, and whether there are any circumstances regarding the candidate's professional indemnity insurance history that may be relevant to the candidate's suitability;
- whether the applicant is capable and willing to comply with the terms of any undertaking given to it by the firm and/or relevant regulators;
- had suitable procedures in place to ensure that insurance monies (money relating to premiums, return premiums and claims) are properly safeguarded;
- whether the applicant possesses all the licences, approvals or authorisations in order to act as a Coverholder wherever it will conduct insurance business in that capacity;
- whether the applicant has suitable and effective risk management (including adequate business continuity, succession and disaster recovery plans).

Particular attention should be paid to the following areas:

The quality and adequacy of the underwriting function

This includes:

- The extent of the Coverholder's knowledge and experience in each type and class of business for which they will be given authority to enter into contracts of insurance and issue insurance documents.
- The quality and adequacy of the Coverholder's control over underwriting, particularly if a number of people are authorised to enter into contracts of insurance or issue insurance documents.
- The limits of the Coverholder's authority. If a new Coverholder is given full underwriting authority, their activities will need to be closely monitored because they may have responsibility not only for accepting risks, but also for setting premiums, in addition to any potential conflicts of interest the granting of such an authority may create. Even when a Coverholder uses pre-determined rates, terms and conditions, close attention will still need to be paid to the risks the Coverholder accepts.

The quality and adequacy of the Coverholder's ability to operate a binding authority

This may include:

- The Coverholder's prior experience, if any, of writing business under a binding authority. If the Coverholder or any distributer in the chain is an unregulated entity, the firm must satisfy itself that this does not result in unfair treatment or poor value to customers.
- How competent the Coverholder's management is and how they propose to manage the binding authority. This will include their ability to monitor service standards, customer outcomes, premium income, claims frequency, claim declinature and repudiation rates, the number of complaints and aggregate exposure limits (where appropriate).
- How the Coverholder proposes to manage any conflicts of interest.
- The Coverholder's internal remuneration arrangements.
- The Coverholder's customer fee charges and fee charging structure.
- The strength of the Coverholder's financial management, including credit control.
- Whether the Coverholder's IT and accounting systems can record and process insurance transactions and produce necessary reports and documents, including management information and reports to local regulators.
- The quality and experience of the Coverholder's staff.
- The location of all staff premises and home workers.
- The Coverholder's other business activities and the extent to which they might divert the Coverholder's attention from the binding authority.
- The Coverholder's understanding of the insurance market and associated regulatory requirements.
- The outcome of any pre-approval Coverholder visit.

The quality and adequacy of the claims handling function

The Coverholder's claims capabilities and procedures should be appropriate for the size and complexity of the Coverholder's business operation, the nature and extent of any claims authority granted, the nature of the business written, any conflicts of interest and the jurisdiction in question, amongst other factors.

However, an insurer may wish to consider:

- Whether it is appropriate to delegate claims authority for that class of business.
- Whether the delegation of claims will affect quality of service.
- The likely type of claims that will be received.

In addition to whether the Coverholder has appropriate:

- Management and other controls relating to claims funds where applicable.
- Staffing levels to cope with anticipated claims activity including average case load per handler.
- Adequate resources to meet the required service standards.
- Management and other controls to monitor staff claims workload.
- Experience levels and qualifications for the personnel involved in claims handling, copies of relevant licences/certificates or regulatory authorisation and appropriate personnel management.
- Procedures for the handling of claims in compliance with any applicable laws and regulations, and in accordance with the insurer firm's expectations.
- Management and other controls relating to claims agreements authority levels and reporting, including claims frequency, claim declinature, repudiation rates and service levels where applicable.
- Conflict management procedures.
- Maintenance and retention of records.
- Litigation management procedures and controls.
- Procedures for the timely settlement of valid claims. Procedures for the timely establishment and reporting of accurate claim reserves.
- Management of third party experts, e.g., adjusters, defence counsel, etc.
- Communication within the Coverholder and with the insurer relating to claims issues.
- Catastrophe claims handling plan in place, where appropriate.
- Adequate E&O/fidelity insurance where applicable.

If an insurer decides to contract any claims handling services to a Coverholder, the insurer is responsible for determining that the authorised party is competent to perform its responsibilities and that the terms of the claims handling contract are consistent with the binding authority. Insurers should be mindful of their regulatory obligations when assessing the adequacy of delegated claims handling authority. Decisions about their claims will be made by parties who have different regulatory responsibilities than the insurer for the outcome and who may have an interest in not agreeing the claim, depending on the remuneration arrangements in place. Firms should also make sure that the contract of delegation clearly sets out the scope of the claims handling authority given to the Coverholder, including clarity regarding who is responsible for driving the claims outcome and any claims matters that are to be reserved for the insurer.

Where an insurer intends to appoint a third party administrator (TPA) (known as Delegated Claims Administrators (DCA) within Lloyd's) to deal with claims, the insurer should ensure that it considers the appropriate suitability criteria and it is recommended that the arrangement is governed through a tripartite contract - see Section 4.8 'Claims/Complaints Handling - Due Diligence of TPAs and Outsourcing Partners'.

The quality and adequacy of the complaints handling function

The Coverholder's complaints handling capabilities and procedures should be appropriate for the size and complexity of the Coverholder's business operation, the nature and extent of any complaints handling authority granted, the nature of the business written and the jurisdiction in question, amongst other factors.

An insurer may wish to consider:

- Whether it is appropriate to delegate complaints handling authority for that class of business.
- Whether the delegation of complaints handling will affect quality of service.

Consideration of whether the Coverholder has appropriate:

- Staffing levels to cope with potential complaints activity.
- Management and other controls to monitor the workload of staff handling complaints.
- Experience levels and qualifications for the personnel involved in complaints handling.

- Procedures for the handling of complaints in compliance with the insurer's complaints philosophy and outcomes, any applicable laws and regulations, and in accordance with the firm's expectations.
- Management and other controls relating to complaints handling service levels and reporting, including complaints frequency, complaints repudiation and upheld rates where applicable.
- Procedures for the timely settlement of valid complaints.
- Conflict management procedures.
- Maintenance and retention of records.
- Procedures for the handling and reporting of complaints.
- Litigation management procedures and controls.
- Communication within the Coverholder and with the insurer relating to complaints.
- Adequate E&O/fidelity insurance where applicable.

Insurers should be mindful of their regulatory obligations when assessing the adequacy of delegated complaints handling authority.

Where an insurer intends to appoint a TPA to deal with complaints, the insurer should ensure that it considers the appropriate suitability criteria and it is recommended that the arrangement is governed through a tripartite contract - see Section 4.8 'Claims/Complaints Handling - Due Diligence of TPAs and Outsourcing Partners'.

The quality and adequacy of the Coverholder's business plan

A new Coverholder will need to prepare a business/underwriting plan for the proposed binding authority. The content of the plan should be agreed with the lead insurer and provide a detailed description of the Coverholder's proposals specific to the business to be written under the binding authority.

The Coverholder's plan should be reviewed as part of the internal due diligence process. The following aspects should be included:

- An explanation of where the business comes from, where it is currently written and why it is moving to the insurer (including possible declinature to renew by previous carrier).
- Consideration of the value the proposed distribution chain will give to the end customer, including any fees charged in addition to the policy premium. It should be noted that disclosure cannot be used as a remedy to manage poor product value.
- Target and historic profitability statistics.
- Details of any other contracts of delegation they manage.
- An analysis of the market place (including opportunities for and threats to successful underwriting).
- The basis for selecting risks.
- The basis for pricing (where appropriate).
- Details of how the binding authority will fit with the Coverholder's other areas of business.

Conflicts of Interest

A conflict of interest is a situation in which the interests of a firm or its employees or persons acting on behalf of the firm, is contrary to the interests of the firm's customers, or where the interests of a customer or group of customers is contrary to the interests of another customer or group of customers. A Conflict of interest may concern a financial benefit as well as any other kind of benefit (including goods or services). Firms must manage conflicts of interest fairly, both between themselves and their customers and between a customer and another client.

Firms should pay careful attention to the duty under the customer's best interests rule (ICOBS 2.1) to act honestly, fairly and professionally in accordance with the best interests of the customer and that any remuneration arrangements, performance assessments or sales targets do not conflict with this duty (SYSC 19F.2). The customer's best interests rule and the management of conflicts of interest

applies equally to firms that delegate authority. Firms should assess each delegated authority agreement for potential conflicts of interest.

The assessment should include the consideration of whether any potential conflicts of interest arise from the delegation of the authority itself, any incentive arrangements, including remuneration and performance management, or the delegation of claims or complaints handling authority. This is particularly relevant where decisions about the claims or complaints are being made by parties who have different regulatory responsibilities than the insurer and who may have an interest in not agreeing the claim or upholding the complaint. Where insurers identify potential deficiencies, they should ensure that these are addressed and appropriately mitigated. The FCA stated in their thematic review of outsourcing arrangements, that profit commission and similar incentives should only be considered where the firm has implemented robust controls to mitigate the conflicts of interest that they give rise to, paying particular heed to SYSC 19F.2.

The key concern in respect of Coverholders will be any circumstance which may give rise (or could be perceived to give rise) to a conflict of interest which may pose a risk of damage to the interests of a policyholder (customer's best interests rule) or underwriters, or which may compromise the objectivity of the Coverholder's performance of its obligations.

Firms should also consider that in the interest of transparency, there may be requirements to disclose to the customer, the nature of the remuneration paid to the firm's employees, which will also include Coverholder and third party administrator staff.

Coverholders that write business on behalf of insurers in a significant number of overseas territories must also comply with any applicable local laws or regulatory requirements, including any that relate to conflicts of interest. Nothing in this Guidance is intended in any way to alter the effect of any local law or regulations that apply to conflicts of interest.

In addition to local laws, the agreement should include an undertaking signed by the Coverholder by which they undertake that they "will manage any conflicts of interest, between ourselves, our customers and the insurer in a fair and open way" (for example the IUA Binding Authority Agreement Model Wording, Section 33).

Therefore, insurers may wish to consider, whether given the particular risk profile of a Coverholder, it needs to provide any further guidance to the Coverholder as to management of potential conflicts of interest, beyond those as required by applicable local laws. There may be situations where a firm considers that a conflict of interest cannot be appropriately managed and chooses therefore not to use a particular Coverholder or distribution method.

Coverholders and Conflicts of Interest

All Coverholders should be aware of the implications of conflicts of interest and in particular they should make sure that they are aware of any applicable laws or regulations that apply to them regarding conflicts of interest. This may include the laws and regulations of its "home" jurisdiction and also the laws and regulations in any other country the Coverholder does business.

The principal party responsible for monitoring compliance with any conflicts requirements is the relevant lead insurer. It should consider:

a) Reviewing the Coverholder's conflicts arrangements as part of the due diligence process in assessing whether to enter into a binding authority;
b) Ongoing due diligence.
c) Coverholder audits. All audits should therefore include whether the Coverholder understands local laws that apply to conflicts and also the suitability of any conflicts arrangements the Coverholder has implemented.

Does the insurer need to give additional guidance?

Whether the insurer needs to provide any additional guidance to a Coverholder will depend on the particular circumstances and risk profile of the Coverholder. Examples where it is more likely that the insurer will want to consider giving additional guidance could include -

Examples of actual conflicts

a) Where the Coverholder also has an interest in the outcome of a service provided to the policyholder or of a transaction carried out on behalf of Underwriters, which is distinct from the policyholder's or Underwriters' interest in that outcome.

b) Where a Coverholder has a financial or other incentive to favour the interest of another insurer over the interests of Underwriters.

Circumstances that could give rise to potential conflicts

a) Where a Coverholder is also a broker, in which case the possibility of a perceived conflict of interest arising is much greater. On the one hand, the Coverholder may have an interest as a broker in placing business on behalf of the policyholder and on the other hand the Coverholder may have a financial interest in binding the risk on behalf of underwriters.

b) Where the Coverholder also has claims settling or complaints handling authority as well as underwriting authority.

What might any additional guidance include?

This will depend on the specific circumstances of the Coverholder but examples could include –

Establishing a "conflicts policy"

The Coverholder may need to establish a written Conflicts of Interest policy to which all of their directors, officers and employees should adhere, to ensure compliance with the relevant local laws and regulations and also with any additional requirements of Underwriters.

In preparing its conflicts policy the Coverholder might wish to consider:

a) Any circumstances which may give rise (or could be perceived to give rise) to a conflict of interest which may pose a risk of damage to the interests of underwriters or a policyholder.
b) Whether there are any circumstances which may cause any individual director, officer, manager or employee of the Coverholder to have any (or any perceived) conflict of interest.
c) The internal arrangements that should be in place to ensure that conflicts do not arise and/or that any conflicts which may arise are properly identified and managed.

Conflict management arrangements

If relevant, given their specific circumstances, Coverholders might need to put in place suitable organisational and administrative arrangements to manage conflicts of interest and ensure those arrangements apply to all key staff. The arrangements will depend upon the scale and complexity of the business and the nature of the binding authority (for example whether the binding authority provides for full rating discretion or is a prior submit binding authority). By way of example, the arrangements could include:

a) Segregating management responsibility in the firm regarding its Coverholder and broking activities.
b) Ensuring that the individuals with responsibility for binding risks should not normally have sole claims or complaints handling authority.
c) Considering whether any additional disclosures should be made.

However, in respect of any conflicts guidance, it is emphasised that the specific arrangements to be put in place for any particular Coverholder will depend upon that Coverholder's circumstances, and before an insurer provides any additional guidance it should first discuss that with the Coverholder to make sure that the proposed guidance is (a) proportionate and (b) is not in conflict with any applicable local laws.

The Coverholder's reputation and standing

The main points to consider when assessing whether or not a Coverholder has an appropriate reputation and standing include the following:

- Regulatory status and current licences.
- Membership of recognised professional bodies.
- Standing in the insurance industry.
- Association with any problems or disputes (for example, with other insurers, Lloyd's or regulators).
- Other types and classes of business they handle.
- Binding authorities they have with other insurers and the Coverholder's performance under them.
- Details of current owners or shareholders.
- Any potential conflicts of interest they may have.

The Coverholder's financial standing

The insurer should conduct a thorough financial analysis of any potential Coverholder. This should include a review of the following:

- A review of at least three years Balance Sheet data and an assessment of working capital, retained earnings and the potential impact of any loans (including repayment terms).
- A review of at least three years Profit & Loss statements, specifically trends in terms of revenues, costs/expenses and profit before tax.
- The Coverholder's involvement in any current litigation or any significant contingent liabilities which may affect their ability to continue to operate (for example, a claim on their errors and omissions insurance).
- The adequacy of the Coverholder's errors and omissions or professional indemnity insurance.

Insurers should consider performing the financial due diligence on an overall financial standing basis as well as a simple credit control basis.

If the Coverholder is a start-up operation, then firms should ask to be provided with a forecast Profit and Loss account covering at least the next three years. An opening Balance Sheet should also be provided for review by the insurer. The insurer should be satisfied that there is adequate provision for cash flow to maintain the start-up. The insurer should document the finding of their financial due diligence in support of the application.

Financial crime and International Sanctions

Insurers have a responsibility to ensure that Coverholders have proper and adequate systems and controls in place to ensure Anti- Money Laundering (AML), anti-bribery and international sanctions compliance. Insurers should also ask specific questions relating to AML/anti-bribery/international sanctions as part of the Coverholder audit process.

However, this does not devolve Coverholders of their own individual responsibilities under relevant legislation (both international and local). Insurers and Coverholders should therefore work together for their mutual benefit, to ensure that adequate systems and controls are in place to fulfil the requisite compliance standards in respect of the class of business undertaken and the Coverholders exposure to the applicable legislation.

The Coverholder's regulatory or licensed status

Any failure by a Coverholder to comply with local regulatory, licensing or tax requirements in a jurisdiction may well have adverse consequences for the insurer in that territory. It is therefore essential that particular attention is paid to licensing requirements when delegating authority to a Coverholder.

An insurer must take reasonable steps to make sure that it and the Coverholder are aware of and implement all relevant insurance, financial and taxation laws and regulations in the jurisdiction where the Coverholder is domiciled, trades, provides services or does business under the binding authority.

Furthermore, an insurer should not assume that because a Coverholder is either a regulated firm or is associated with the insurer (i.e. as its Appointed Representative), that a binding authority with such a Coverholder implies a reduction in operational risk.

The Coverholder's E&O Coverage

In terms of scope of cover, the insurer should obtain evidence that the policy is in force at the time approval is granted and that it specifically includes activity as a Coverholder (or refers to "underwriting" or "MGA" etc.), including claims and/or complaints handling activity where necessary. The insurer may require sight of a copy of the full policy wording/endorsements or confirmation from the carrier to ensure this is the case and that no exclusions apply. There should be documented evidence on file of how adequacy is determined.

With regards to policy limit, the adequacy should be determined initially by the insurer, taking into account a number of factors including the size of the Coverholder's operations, the Coverholder's historic claims experience under its E&O coverage, any assessments produced in recent audit reports and the competence and experience of key personnel. A firm may not require a Coverholder to purchase professional indemnity limits that match high binding authority contract limits but this should also be a consideration when assessing the adequacy of the professional indemnity limits purchased. Please be aware that in certain territories, including the UK and the EEA, rules exist regarding minimum limits.

Coverholders with several binding authorities or facilities present a higher risk of limit erosion and therefore firms should consider imposing a minimum aggregate limit. Firms should also consider including in the due diligence of applicants with high professional indemnity deductibles, research into the reason for this and an assessment of its ability to cover the monetary amount out of cash reserves or realisable assets.

When adding an additional class of business, firms should satisfy themselves that the professional indemnity limit remains adequate for the increased binding authority limit.

Firms should also take into consideration the security rating of the E&O insurer.

Coverholder Employees Working away from an Approved Office

Coverholders are increasingly able to quote and bind risks remotely (e.g. whilst at home) via the use of laptops and remote internet connections. This may be from a home address or other unapproved location.

Insurer(s) may be of the view that this activity falls within the approval status of the Coverholder and may wish to consider if:

- The unapproved address is not advertised as a business workplace and it does not feature on any business correspondence.
- The remote worker is and remains an employee of the approved Coverholder.
- The IT systems being used are the same as and are linked to the approved office systems.
- Appropriate controls are in place to maintain data security.

- The use of remote workers is in compliance with the terms of the binding authority.
- Documents are not signed or issued from the remote address.

Issues may arise where a worker is based away from an approved office and is formally carrying out Coverholder activities with the agreement of their employer.

The risks that might occur are numerous and include - lack of supervision, use of unauthorised IT systems, data breaches, issuing incorrect documents, lack of appropriate licence if resident in a different state/province, not included in PI coverage, non-compliance with reporting requirements including bordereau and policyholders sending premiums to the unapproved address. In addition, care needs to be given as to whether the location of the remote worker could be considered as an establishment for tax or regulatory purposes.

If an employee works from a remote unapproved address, rather than the approved Coverholder office, the employee should be recorded.

No Coverholder activity (even occasional) should be permitted unless:

- The IT system accessed is the same as and directly linked to the Coverholder office to enable supervision of activities such as quoting and binding.
- Where the remote address is located in a different state/province/country to the Coverholder the insurer has satisfied itself that there are no issues as far as the requisite licences are concerned. This applies equally on the part of the Coverholder's local regulator or the local regulator in the state/province/country of the remote address.

In addition, the insurer should be satisfied that:

- They have considered whether there are any regulatory or taxation implications as a result of agreeing to the remote worker. (It may be that in certain cases the insurer may need external independent advice).
- The individual has clear, agreed and understood levels of authority and is an employee of the Coverholder.
- The Coverholder/employer has carried out a risk assessment and has implemented appropriate controls.
- There is evidence of effective controls in place.
- The remote worker does not handle or account for insurer monies from the remote location.
- There is a clearly stated review process for the activities of all authorised remote workers.
- The address is not an office which should be approved.
- The professional indemnity insurance will cover the remote worker/remote address.
- The arrangement is examined and tested as part of the internal audit programme.
- The insurer's own audit programme will cover this aspect.

4.4 Oversight, Monitoring and MI

Insurers outsourcing functions or tasks need to organise and control their affairs responsibly and effectively, and to have in place appropriate systems and controls to manage the operational risks outsourcing gives rise to, including any risks around treating customers fairly. Sections 6 and 7 provide more detail in respect of the management of binding authorities and conduct risk considerations.

4.5 Due Diligence at Renewal & Material Changes

Insurers should ensure that the due diligence is kept up to date throughout the life of the binding authority. In addition to ongoing due diligence, a reassessment of the delegated authority should occur at renewal of or at the time of any material change to the agreement.

Renewal provides one opportunity to update the information a firm has on the Coverholder. However, by carrying out its updated due diligence process at this time, it can create an additional 'bottleneck'

in the process at an already busy time when the binding authority is being renewed. Accordingly, firms may wish to consider updating the information they have on the Coverholder outside of the renewal period. This will allow the due diligence performed by the insurer at renewal to be proportionate and appropriate based on the level of due diligence carried out on an ongoing basis. In these cases, the due diligence should be limited to enquiries that are relevant to any areas where changes that are proposed for the next period of the binding authority. Where the insurer can evidence sufficient ongoing due diligence, then the level of the review upon renewal should reflect this accordingly.

Renewal or material changes also provide an opportunity for the firm to consider whether the existing relationship is still consistent with their risk appetite and delegated authority strategy.

4.6 Following Insurers

Insurers considering following a lead on a binding authority with a new Coverholder need to satisfy themselves that effective due diligence has been undertaken and must make their own decision as to the suitability of the Coverholder, including:

- Determining and articulating, within their Delegated Authority procedures, a policy regarding the extent of due diligence that they will carry out themselves in respect of follow business. This may take into account, for example, class of business, extent of delegation (underwriting, claims and/or complaints) and premium income.
- Evidencing that this due diligence has been carried out, and signed off appropriately, for audit trail purposes.

The regulator expects any firm that is considering entering into a follow relationship with a lead underwriter to understand the reasons for entering into such a relationship and have good grounds for doing so. The follower must also have systems and controls in place to monitor the arrangement, including claims and complaints data, so that the firm is satisfied that the lead is managing the arrangement appropriately.

4.7 Sub-delegation and supply chains

Some delegated authority arrangements allow for the Coverholder to sub-delegate the arrangement to another party. Firms must ensure that appropriate due diligence is undertaken for all parties in the chain, including any sub-delegation arrangements and that appropriate oversight and control is maintained by the firm. Firms may choose to rely on some information that has been provided by an entity in the chain. However, firms must be satisfied that the entity is familiar with the regulatory requirements, the firm has sight of the information collected and is satisfied that a thorough due diligence process has been conducted, at least to the same standard that the firm itself would have undertaken.

In the course of handling claims and/or complaints for insurers, some intermediaries also sub-delegate elements of claims/complaints handling to third party providers. Additionally, in some cases both intermediaries and third parties manage extensive service provider networks or customer helplines involved in the claims/complaints handling process.

The involvement of additional parties can provide a further challenge in being able to demonstrate control over outsourced claims/complaints processes and outcomes. Insurers should be able to evidence the standards and processes in place to manage these agreements, including evidence of value to the customer. It is recommended that these arrangements are managed through tri-partite agreements.

4.8 Claims/Complaints Handling - Due Diligence of TPAs and Outsourcing Partners

Where the insurer decides to appoint a separate TPA or outsourcing partner to handle claims/complaints then the insurer should assess the proposed firm against suitability criteria which may include:

Table 4.8

a) the applicants compliance with appropriate principles of good corporate governance;
b) if they are a competent, proficient and capable organisation (taking into account the needs of the insurer);
c) the knowledge and experience of the applicant's directors, officers and staff regarding the conduct and regulation of claims/complaints insurance business, including in any other relevant jurisdiction;
d) the quality and adequacy of the applicant's other resources, including the quality and adequacy of the applicant's systems, procedures, protocols and arrangements for the conduct of its business;
e) the nature of the TPA's/outsourcing partners business, including its past performance and any past relationship with the firm;
f) whether they have suitable resources for the determination of claims and/or for handling complaints including resources to ensure compliance with the terms of the claims/complaints agreement and any appropriate service standards including those for customers;
g) whether they have suitable internal procedures and processes for the administration and agreement of claims or complaints handling (including procedures for the appointment of experts, litigation management and file retention) and that those are properly documented and made available to all relevant directors, officers and staff;
h) whether they have suitable systems and procedures to record and report management information to the insurer in respect of its performance of its obligations under the claims/complaints agreement;
i) are they able on a timely basis to properly assess and review claim estimates;
j) are they able to review and settle complaints on a timely basis;
k) whether they have suitable arrangements for identifying, resolving or managing conflicts of interest. This includes where the firm or any of its directors, officers or staff have or will have authority to enter into contracts of insurance or have or will have any financial interest in an entity that may give rise to circumstances that may constitute a conflict of interest);
l) whether the candidate maintains appropriate levels of data security (with a consideration of any third-party IT services used, including cloud based solutions) and that it complies with any applicable data protection legislation;
m) whether they have suitable and effective risk management (including business continuity and succession plans), internal control and internal audit processes;
n) the TPA/outsourcing partner and its directors, officers and relevant staff are of suitable competence, reputation and character;
o) or any controller of the firm is of appropriate reputation and standing;
p) whether they have adequate professional indemnity insurance and whether there are any circumstances regarding the candidate's professional indemnity insurance history that may be relevant to the candidate's suitability;
q) whether they have adequate capital and financial resources;
r) whether they have suitable procedures in place to ensure that insurance monies (money relating to premiums, return premiums and claims) are properly safeguarded;
s) whether the TPA/outsourcing partner is capable and willing to comply with the terms of any undertaking given to it by the insurer, Coverholder and / or relevant regulators; and
t) whether they possess any necessary licences, approvals or authorisations in order to act as a third party administrator or outsourcing partner wherever it will conduct business in that capacity.

SECTION 5 - CLEAR, CONSIDERED AND COMPLETE BINDING AUTHORITIES

5.1 Introduction

Insurer(s) should ensure that there is a contract certain binding authority contract in place, prior to inception of the arrangement. In order to achieve this, insurers should consult and comply with the relevant provisions outlined in section 4. Insurers should also ensure they comply with the Contract Certainty Code of Practice (October 2012), published by the London Market Group.

Lead insurers of lead/follow arrangements should ensure that contracts have been agreed, signed and dated by all parties (including the Coverholders to whom authority is delegated) prior to inception of the contract.

Insurers should ensure that where there is a series of wholesale or retail producers in the chain who will bind insurances and/or issue documents, the Coverholder has the relevant TOBA arrangements in place and that the capacity each link in the chain is acting in is clarified in the relevant agreement. The insurer should also have oversight of the Coverholder's control of these activities.

5.2 Requirements for the content of contracts of delegation

All binding authorities

Every binding authority or where appropriate, the line slip, should contain the details found in **Table 5.2 A**.

Where a groups of individuals on the Coverholder's staff will be given authority to bind risks, e.g. call centre arrangements, it is permissible to identify the Underwriting Director/Call Centre Manager or Chief Underwriting Officer or other key staff. In such a case the binding authority should state that the named individuals have overall responsibility and control of underwriting and document issuance. It should also make clear that they may delegate authority to other employees in accordance with guidelines agreed with the insurer and detailed in the agreement (either in the main agreement or appended in line with internal policy). This must be agreed in writing by the underwriters in advance and said authorities are made available to underwriters on request. In addition, all locations in which the Coverholder operates should be stated to the underwriters as well as any authorised remote workers.

Table 5.2 A

1) an agreement number or reference number;
2) the name and address of each party to the binding authority;
3) the name and address of each broker which is a party to the binding authority or which arranged or brokered the binding authority;
4) the period;
5) the name of the Coverholder's director or partner or an authorised individual at the Coverholder who is directly responsible, on behalf of the Coverholder, for the overall operation and control of the binding authority;
6) the names of the Coverholder's directors, partners or employees who will have authority to enter into contracts of insurance under the binding authority;
7) the names of the Coverholder's directors, partners or employees (if any) who will have authority to issue documents evidencing contracts of insurance under the binding authority;
8) a list of the terms and conditions which must be incorporated in contracts of insurance entered into under the binding authority including:
    a) relevant wordings, exclusions and limitations;
    b) the maximum period of cover;
    c) the limits of liability (other than where inclusion of such a limit would be contrary to any applicable law); and
    d) any applicable territorial wordings or general cover conditions;
    e) the law and jurisdiction applicable to the contract of insurance.
9) a precise description of the nature or classification of the contracts of insurance that the Approved Coverholder or slip leader will be authorised to enter into and any relevant exclusions and limitations;
10) details of the manner by which any insurance monies are to be held, maintained and properly safeguarded;
11) the manner or basis for the calculation of premiums, discounts, commissions, brokerages, fees, charges and expenses and a description of services to which they relate;
12) the maximum aggregate premium income limit in respect of all contracts of insurance that the Coverholder may enter into;
13) the maximum limits of liability in respect of contracts of insurance that the Coverholder may enter into;
14) the territorial limitations on the Coverholder's authority;
15) provisions that set out the capacity under which the Coverholder is acting with regard to a product co-manufacturer and/or distributer role and clear details of the relevant responsibilities for each party;
16) provisions that set out the capacity under which the Coverholder is acting in respect of data protection, and the data breach requirements, including notification responsibilities;
17) provisions requiring the Coverholder to report in respect of all premiums, paid claims, outstanding claims and expenses in respect of contracts of insurance entered into by class or category by the Coverholder under the binding authority;
18) provisions setting out how and when the payment and settlement of monies due from each of the parties to the binding authority or line slip should be made;
19) provisions for the amendment, cancellation and termination of the binding authority or of the line slip by the parties;
20) provisions that consider ownership of the customer and intellectual property rights (including IT systems), particularly in the event of cancellation or termination of the binding authority;
21) provisions clearly stating the Coverholders commitment to comply with all applicable laws, regulatory requirements and guidelines and to cooperate with the insurers supervisory authority;
22) provisions relating to the ongoing obligations of the Coverholder in the event that the binding authority expires or is terminated or cancelled for any reason;
23) provisions setting out the jurisdiction and governing law that relates to the operation of the agreement and for the settlement of disputes arising from the binding authority or line slip;
24) provisions requiring the Coverholder or the third party administrator or any of its directors or staff to meet any relevant professional competence standards (including minimum CPD requirements);

25) provisions requiring the Coverholder or the third party administrator to maintain records and documents in such manner and for such period as the insurer may require or as may be required by any applicable legal or regulatory provision;
26) provisions regarding the maintenance and security of confidential information;
27) provisions requiring the Coverholder or the third party administrator to respond to questions addressed directly to it by the insurer's supervisory authority;
28) provisions requiring the Coverholder or the third party administrator to allow the insurer, any auditor or agent appointed by the insurer or the insurer's supervisory authority, effective access to all information, documents, books, records and other materials, including carrying out on-site inspections (which will include the premises of any third-party IT service, e.g. cloud based solutions), which, in the opinion of the insurer relate or purport to relate to the operation of the agreement and to co-operate with the insurer, auditor, agent or insurer's supervisory authority;
29) provisions requiring the Coverholder or the third party administrator to produce to any relevant regulatory body any information, documents, books, records and other materials which in the opinion of the relevant regulatory body relate or purport to relate to the operation of the agreement;
30) provisions requiring the Coverholder or the third party administrator to notify the insurer of any:
    a) complaint or actual, pending or potential litigation;
    b) circumstance or development that may materially impact upon its ability to perform its functions under any part of the agreement effectively and in compliance with applicable laws and regulations;
31) provisions prohibiting the Coverholder or the third party administrator from subcontracting or assigning any of its rights, powers, functions or obligations under the agreement without the prior consent of the insurer;
32) provisions stating that the Coverholder's or third party administrator's duties and responsibilities remain unaffected by any subcontracting that has been agreed to by the insurer under (29);
33) provisions that govern internet selling, if applicable.

Line slips (Bulking or Non-Bulking)

In the case of contracts of delegation that are line slips, the line slip agreement must also contain:

Table 5.2 B

1) the name and address of the broker responsible for placing or administering the line slip;
2) the authorised insurance companies that are delegating authority to enter into contracts of insurance and (if any); the syndicate or syndicates on whose behalf each Managing Agent is delegating authority to enter into contracts of insurance (the "syndicates");
3) the authorised insurance company or the Managing Agent that is authorised to enter into contracts of insurance under the line slip (the "slip leader");
4) provisions to ensure that each of the parties to the line slip receive information relating to the operation of the line slip including, in respect of each contract of insurance entered into under the line slip, details of the name of the insured, the sum insured, the premium charged and the period of the contract of insurance;

Binding authorities that delegate claims authority

Any agreement where the insurer has delegated authority to determine claims arising under contracts of insurance to a Coverholder, third party administrator or outsourcing partner should contain the following information, provisions and terms and comply with the following conditions and requirements:

Table 5.2 C

1) the name of any person who will have authority to agree claims made on contracts of insurance entered into by the Coverholder under the binding authority;
2) the name and address of each party to the agreement that the insurer is delegating authority to determine claims arising under contract of insurance;
3) the functions, duties and responsibilities of the Coverholder, third party administrator or outsourcing partner that are relevant to its authority to determine claims. This shall include –
   a) the level of the Coverholder's, the third party administrator's or outsourcing partner's authority to determine claims (including the circumstances in which a claim shall be referred to the insurer);
   b) details of the Coverholder's, the third party administrator's or outsourcing partner's responsibility to investigate claims and where appropriate appoint external experts (including the circumstances in which the decision to appoint an external expert shall be referred to the insurer) and take steps to ensure claims are defended as appropriate and to seek to make any recoveries;
   c) details of the Coverholder's, the third party administrator's or outsourcing partner's responsibility to assess and review claim estimates;
   d) details of any applicable service levels or standards (including service standards for dealing with complaints and enquiries);
4) provisions requiring the Coverholder, third party administrator or outsourcing partner to report to the insurer in respect of paid claims, outstanding claims and expenses in such form and at such intervals as the insurer may determine;
5) provisions for the cancellation and termination of the agreement;
6) provisions relating to the ongoing obligations of the Coverholder, third party administrator or outsourcing partner in the event that the agreement expires or is terminated or cancelled for any reason;

It is likely to be particularly important that the insurer considers including the following provisions, as appropriate:

- Clarity as to which claims are within the scope of the delegation of authority.
- Clarity as to those claims or claims matters that are referred to the insurer for decision for any reason.
- A description of the responsibilities of the Coverholder, third party administrator or outsourcing partner as regards those claims that are within the scope of its authority including: the investigation of claims, coverage review, defence of the insured (where applicable), timely and accurate reserving, the appointment and management of appropriate experts where required, timely and proper claim payments (where applicable), responding to enquiries and complaints, investigating potential recoveries and reporting to the insurer.

Binding authorities which delegate complaints handling authority

Any agreement where the insurer has delegated authority to determine and handle complaints arising under contracts of insurance to a Coverholder, third party administrator or outsourcing partner should contain the following information, provisions and terms and comply with the following conditions and requirements:

Table 5.2 D

1) the name of any person who will have authority to investigate and settle complaints made on contracts of insurance entered into by the Coverholder under the binding authority;
2) the name and address of each party to the agreement that the insurer is delegating authority to determine complaints arising under contract of insurance;
3) the functions, duties and responsibilities of the Coverholder, third party administrator or outsourcing partner that are relevant to its authority to determine complaints. This shall include –
   a) the level of the Coverholder's, the third party administrator's or outsourcing partner's authority to determine complaints (including the circumstances in which a complaint shall be referred to the insurer);
   b) details of the Coverholder's, the third party administrator's or outsourcing partner's responsibility to investigate complaints;
   c) details of any applicable service levels or standards;
4) provisions requiring the Coverholder, third party administrator or outsourcing partner to report to the insurer in respect of settled complaints, outstanding complaints and redress in such form and at such intervals as the insurer may determine;
5) provisions for the cancellation and termination of the agreement;
6) provisions relating to the ongoing obligations of the Coverholder, third party administrator or outsourcing partner in the event that the agreement expires or is terminated or cancelled for any reason;

It is likely to be particularly important that the insurer considers including the following provisions, as appropriate:

- Clarity as to which complaints are within the scope of the delegation of authority.
- Clarity as to those complaints or complaint matters that are referred to the insurer for decision for any reason.
- A description of the responsibilities of the Coverholder, third party administrator or outsourcing partner as regards to those complaints that are within the scope of its authority including: the investigation of complaints, timely and proper settlement, responding to enquiries and complaints within agreed timescales and reporting to the insurer.

In addition to the above areas there are other matters which the insurer should ensure are covered in the contract.

Premium settlement

The Coverholder is usually responsible for collecting premiums on behalf of the insurer. The binding authority contract must clearly set out the Coverholder's responsibilities in terms of bordereau format, reporting and settlement frequency.

Insurance monies

It is essential that the Coverholder understands that insurance monies are held on behalf of underwriters. Coverholders must hold that money in a separate insurance monies account, separate to their own business accounts. In many jurisdictions, that separate account must be a trust account. Even where this is not required, the use of trust accounts is strongly recommended. This is important to protect policyholders' funds if the Coverholder becomes insolvent.

In addition, insurers should endeavour to secure a "no set-off" letter from the bank at which the Coverholder's premium account is held.

Whether a firm chooses to allow their Coverholders to co-mingle premiums with other insurers and/or policyholders or requires a separate, segregated or ring-fenced bank account, this should be reflected in the binding authority agreement. The FCA requirements on client money arrangements can be

found in the Handbook under CASS 5.

It is essential that the Coverholder's responsibilities and appropriate service standards are clearly set out in the agreement in relation to the collection of premiums.

Inspection and ownership of records

The binding authority must require the Coverholder to keep complete records of all the business the Coverholder writes as well as claims/complaints reported under the binding authority. It should also make clear that the insurer(s) retain full title to, and ownership of, all of these records, including the paper files if so required.

Insurers, their representatives and regulators, must have the right at any time without restriction or limitation, to inspect, audit and copy any records relating to contracts of insurance accepted by the Coverholder.

Limits on premium incomes

The binding authority must specify a limit on the gross annual premium income to be written under the contract. This is an important control and, used effectively, can prevent a Coverholder from writing more business than the insurer wants. It is essential that the insurer sets the limit at a realistic level. In some cases, it may also be appropriate for the insurer to specify a premium income limit by a sub-class of business or by Coverholder (for example, for multi-class or multi-Coverholder contracts with significant premium income limits).

The insurer should also make sure the Coverholder tells it once the overall written premium income exceeds a set percentage of the overall gross annual premium limit stated in the binding authority (for example, 75% of the agreed gross premium limit). This gives an early warning of any potential overwriting on the contract.

If the binding authority contains a provision to allow a portfolio transfer at the end of the period, the insurer should consider the premium income limit and aggregate exposures if the transfer does not take place.

Internet selling

If the Coverholder is to be permitted to bind contracts online, then that must be clearly stated in the binding authority. Section 4.2 of the IUA Binding Authority model wording states that underwriters must agree in advance to any internet trading carried out by a Coverholder. If the Coverholder is intending to offer insurance over the internet, the insurer will need to be satisfied that this is allowed locally. In this situation, the insurer should have approved the relevant aspects of the Coverholder's website before the Coverholder offers the insurance on their behalf. Relevant aspects include:

- Approval of the arrangements in place for data privacy and security
- Approval of site developers
- Up to date service level agreements in place between the developer and the Coverholder
- Regular site maintenance

For further requirements in relation to internet selling see also section 1.7 of the IUA Binding Authority model wording.

Financial Crime, Sanctions and Anti-Bribery Requirements

The binding authority should include a clear clause setting out the Coverholder's obligations to avoid the risk of financial crime and to avoid risk of breaching any applicable international sanctions, anti-money laundering requirements or any anti-bribery requirements.

The model IUA Binding Authority wording contains a financial crime clause at Section 34.

Conflicts of interest

The binding authority should have clear provisions to deal with the management of conflicts of interest (see Conflicts of Interest in Section 4). The binding authority should ensure that the Coverholder must have no conflicts of interest that may impair the Coverholder's performance of duties under the agreement. The agreement should be assessed for potential conflicts of interest and should include consideration of whether any potential conflicts of interest arising from incentive arrangements are appropriately mitigated. Where firms identify deficiencies, they should ensure that these are addressed appropriately.

Coverholders that write business on behalf of insurers in a significant number of overseas territories must also comply with any applicable local laws or regulatory requirements, including any that relate to conflicts of interest. Nothing in this Guidance is intended in any way to alter the effect of any local law or regulations that apply to conflicts of interest.

In addition to local laws, the agreement should include an undertaking signed by the Coverholder by which they undertake that they "will manage any conflicts of interest, between ourselves, our customers and the insurer in a fair and open way" (for example the IUA Binding Authority Model Wording Section 33).

Confidentiality and data security

It is important that the binding authority sets out clear provisions to ensure that the Coverholder protects confidential information of the insurers and of clients/policyholders and that it complies with its obligations under the relevant local data protection legislation. This applies equally whether as data controller or data processor (as appropriate). The term "local data protection legislation" shall include all applicable statutes and regulations in any jurisdiction pertaining to the processing of personal data, including the privacy and security of personal data. Where Coverholders, TPAs or outsourcing partners use third-party IT services such as cloud based solutions, consideration should be given as to whether the third-party IT service provider will allow access, including physical access, to the premises which are relevant to the contract.

Regard should also be had to information ownership rights – see inspection and ownership of records above.

Business continuity

The binding authority should include a clear statement of the Coverholder's obligations to maintain and implement an adequate business continuity and disaster recovery plan to ensure that the Coverholder can continue to perform its obligations under the agreement. Firms may wish to include any service level agreement measures that they require or have agreed with the Coverholder in the contract.

Termination provisions

The insurer must carefully consider the provisions for terminating the contract of delegation. It will rely on these provisions if it needs to cancel the contract quickly and to make sure the Coverholder does not abuse the contract after notice of termination has been given.

The termination provisions should allow:

- The contract to be terminated immediately upon fraud or dishonesty or if any relevant regulator has directed that it is cancelled.
- The insurer to terminate the contract if the Coverholder's ability to carry out its obligations under the binding authority are materially impaired.

- The insurer to terminate the contract, for any reason, after giving the agreed number of days' notice.
- Extra controls and/or restrictions to be placed over the Coverholder during the notice period. For example, the contract of delegation may revert to a more restricted form of delegation, taking into consideration any lead insurer agreements and following markets, including where a firm is acting as the lead.
- Takeover and ownership of files (including paper files if required), data and any tools or instruments for the purpose of undertaking the delegated authority.

Careful consideration should be given to setting the applicable notice period that the Coverholder can give to terminate the binding authority. It is important that any notice period that the Coverholder can give is long enough to allow the insurer to find an alternative arrangement.

The binding authority should also set out the duties of the Coverholder once termination notice has been given. For example:

- The ongoing conduct risk duties
- Returning insurance documents
- Providing access to underwriting and claims records
- Expenses and charges
- Tacit renewals
- Local legislation
- Claims and complaints administration
- Data retention and deletion requirements

A 'suspension' provision may also be included in the contract of delegation. This provision will allow the insurer to stop the Coverholder from entering into contracts of insurance, issuing insurance documents, handling complaints or paying claims. The provision is likely to be of most use when serious irregularities are brought to the attention of the insurer and will allow time for the matter to be investigated.

Any extra controls that are placed over the Coverholder during the suspension period should take into consideration any lead insurer agreements and following markets, including where a firm is acting as the lead.

Delegating authority to the slip leader

Where a binding authority agreement provides for the delegation of authority to the slip leader to agree amendments to the binding authority agreement, this should be subject to clearly defined limits. Unlimited or excessive levels of delegation to a slip leader are considered unacceptable and pose regulatory and operational risks to the following underwriters.

Insurers must ensure that any clause delegating authority to the slip leader to agree amendments to the binding authority agreement clearly sets out the scope and limits of the slip leader's authority. The clause should not purport to give the slip leader unlimited authority to amend the terms of the binding authority or allow the slip leader an unlimited ability to accept special acceptances. Delegation of authority should be limited to agreeing non-material amendments.

Hold harmless clauses

Hold harmless clauses would require the Underwriters to indemnify and hold harmless the Coverholder in respect of any claims that may be brought by third parties arising from the Coverholder's negligent operation of the binding authority. They also prevent Underwriters from seeking any legal redress against the Coverholder for breaching the terms of the binding authority, other than in very limited circumstances.

It is recognised that as part of the commercial negotiation of a binding authority agreement parties may wish to negotiate limitations of liability. The level of any limitations will depend upon a number of

factors including the nature and scope of the delegation of authority, the class of business that may be bound and the risk appetite of the insurer.

Jurisdiction and choice of law

The binding authority should include a clear statement of the applicable law and jurisdiction and that this is consistent with any arbitration clause.

5.4 Preparation of the contract – sources of information and assistance

In preparing the contract of delegation, regard should be had to the guidance issued by the London Market Group. Practical assistance can also be obtained from other sources as detailed below.

The London Market Group template and guidance

The London Market Group has issued a set of mandatory templates – Market Reform Contracts (MRCs) – that must be used when drafting the binding authority agreement.

MRC templates are updated periodically. Guidance is available on how to use the templates covering the following:

- Definition of the Slip Headings
- Stamp / Line conditions
- Requirements for Contracts of Delegation
- Expert Fees Collection
- FCA Client Classification
- Unique Market Reference Guide.

These guidelines and templates can be found at www.londonmarketgroup.co.uk.

The binding authority guidelines were designed to align with the Contract Certainty Code of Practice guidance issued by the London Market Group (LMG).

IUA Binding Authority Model Wordings

The IUA has also issued binding authority model wordings and guidance notes to assist in the wording of the contract. These wordings are also updated periodically and the most recent versions can be found on the clauses section of the IUA website at www.iua.co.uk. The MRC slip templates are compatible with new model wordings. The LMA also have their own model wordings. There is no requirement for insurers to use the model wordings.

5.5 Submission to Xchanging

Where processing via central settlement and/or the recording of reporting information is required, the binding authority contract should then be submitted to Xchanging. Xchanging will not process a contract of delegation unless there is clear evidence that the insurer and Coverholder have both agreed the contract of delegation before the Coverholder is authorised.

The Market Reform Contract (Binding Authority), including the schedule to the main wording, and insurer numbers and signed lines will be required by Xchanging to enable them to carry out their post-bind quality assurance check and allocate an FDO (For Declaration Only) signing number.

For contracts that incorporate one of the model wordings, there is no requirement for the text of the wording to be provided to Xchanging. However, if the insurer (or the broker) specifically wishes to have the full Binding Authority signed and embossed, then the full number of copies and the model wording will need to be submitted.

An initial London Premium Advice Note (LPAN) is completed with all relevant details by the broker for the FDO signing of the binding authority itself, and subsequent LPAN / Lloyd's Claims Collection Form (LCCF) presentations are then made in the form of bulked submissions on a monthly, quarterly or as agreed basis in accordance with the binding authority contract. Xchanging will carry out checks with respect to premium and claims processing information (e.g. Risk Code) and necessary closing information.

5.6 Contracts with multiple sections with different leads

Some binding authority agreements are written with multiple sections each with a different lead. When writing a contract like this it is important that each section clearly sets out the authority being granted under it and to whom it is being granted. Any other particulars relevant to that section should also be clearly stated.

It is a requirement of the regulatory rules that product manufacturer responsibilities are clearly allocated and managed appropriately. With different leads, it is imperative that it is clearly set out in the contract as to which firm is the manufacturer for each section and that the various responsibilities are allocated accordingly. We would expect in these cases that the multiple leads will all be co-manufacturers, however, firms may agree that one firm or lead will have overall responsibility for the co-ordination of manufacturer roles and maintain oversight and control of the process. Consideration will also need to be given to termination provisions, especially in cases where a lead of a section may wish to terminate the agreement or the firm with overall responsibility no longer wishes to undertake this role. (See Section 9 – 'Non-Renewal and Termination')

SECTION 6 - INSURANCE DOCUMENTS

6.1 Introduction

The firm must be satisfied with the format and content of the insurance documents the Coverholder will issue under the binding authority and should hold the agreed format for this on file.

To satisfy the requirements of the Contract Certainty Code of Practice (Principle B) with regard to the prompt delivery of insurance documents, insurers should require each Coverholder to confirm that insurance documents have been issued within required timescales. The form and frequency of this return from Coverholders should reflect the insurer's assessment of risk, while ensuring that returns are received at least annually from each Coverholder.

6.2 Content of insurance documentation (see also Section 5)

Insurance documentation evidencing contracts of insurance issued by a Coverholder should include the following information, provisions and terms:

Table 6.2

1) the name and address of the Coverholder;
2) all relevant terms and conditions that relate to the contract of insurance entered into by the Coverholder including:
   a) relevant wordings, exclusions and limitations;
   b) the maximum period of cover; and
   c) the limits of liability.
3) if required, the relevant Insurance Product Information Document (IPID);
4) the amount of the premium and any other information relating to the cost of the contract of insurance that is required by applicable laws or requirements to be disclosed;
5) information about the procedures for handling claims arising under the contract of insurance and for the resolution of complaints;
6) the law and jurisdiction applicable to the contract of insurance; and
7) any other provisions required under the laws or requirements of the jurisdiction in which the contract was concluded, including any required data privacy notice, where the insured is domiciled or of any other relevant jurisdiction and any other provisions as required by the relevant representative or agent.

Where a binding authority model wording agreement is used, the insurance document should include the information as specified in the Format and Content of Contract Documentation section (section 20). If a firm uses its own binding authority wording agreement, then the insurance documentation should include any information as specified by the agreement. Firms should also include any information that is required by the law or regulation of the local jurisdiction.

The insurer should also ensure that every insurance document issued to a policyholder contains an appropriate several liability clause. This applies whether or not the binding authority is entered into by one or more insurers.

The London Market Group has produced a Decision Chart (November 2012) for identifying the appropriate several liability clauses to be used both for binding authorities and insurance documents issued to policyholders.

6.3 Combined (“Joint”) Certificates

From time to time, firms may wish to permit their Coverholders to issue “combined certificates” to policyholders (i.e. a single certificate that evidences a contract of insurance in which a proportion of the security is to be provided by insurers other than the firm, which may also include members of Lloyd’s.) These are also often referred to as “joint certificates”.

Firms should only permit combined certificates to be issued where they believe it to be appropriate and prudent so to do and also include the appropriate joint and several liability clause.

Where a model wording binding authority agreement is used, the insurance document should include the information as specified in the Additional Requirements for Combined Certificates section (section 20). If a firm uses its own binding authority wording agreement, then the combined certificate should include any information as specified by the agreement. Firms should also include any information that is required by law or regulation in the local jurisdiction.

SECTION 7 - ONGOING MANAGEMENT

7.1 Introduction

Insurers, lead or follow, should monitor the performance of all Coverholders, TPAs or outsourcing partners to whom they have delegated authority. To monitor performance, firms should specify what information the Coverholder, TPA or outsourcing partner is required to provide, and its frequency, within the binding authority.

Insurers outsourcing functions or tasks need to organise and control their affairs responsibly and effectively, and to have in place appropriate systems and controls to manage the operational risks outsourcing gives rise to, including any risks around treating customers fairly.

7.2 Internal resources

An insurer must retain the necessary expertise to supervise all Coverholders effectively and to manage the risks associated with Coverholders. Therefore, the insurer must demonstrate that it has the necessary internal resources to monitor the contracts of delegation, for example through an in-house binding authority management team. This team should:

- Have skills and experience suitable to manage the dimensions of the binding authority portfolio
- Have a clear set of policies and procedures, defining roles and responsibilities and
- Have a clear structure for management reporting

In the absence of such a team, an individual with an audit and Coverholder business background could perform binding authority management activities.

Resources should include an effective IT system, commensurate with the number and complexity of the binding authority involved, especially the number of lead contracts.

Effective monitoring can be achieved through:

- Internal written procedures describing the processes, areas of responsibility and systems to be used in monitoring and renewing contracts
- Procedures describing requirements and responsibilities as regards to conduct focussed monitoring relevant to the outsourcing relationship and the product
- Procedures describing requirements and responsibilities as regards credit control monitoring
- A suite of exception reports and root cause analysis to enable senior management to address key issues
- An effective annual Coverholder audit programme, and a systematic follow up of report recommendations
- Establishing a formal committee which has responsibility to the firm's Board to oversee delegated authority issues

7.3 Reporting risks, premium, claims and complaints

Coverholders must report regularly, in line with the insurer's reporting requirements and the class of business, on risks they have written, premium payments, claims and complaints. This will allow the internal resource to maintain oversight and ongoing monitoring of the binding authority adequately.

Compliance with the Binding Authority – Management Information

Effective and regular reporting and submission of management information (MI) by the Coverholder, TPA or outsourcing partner is key to enabling the insurer to monitor compliance with the binding authority agreement. It also ensures consistency of approach, service level standards, conduct risk and customer outcomes. Analysis of the information requested should enable the insurer to assess the completeness of the information provided and dictate any follow-up actions required. It is

important that the outputs of any monitoring and MI are reviewed, understood, shared as necessary and acted upon. The MI needs to encompass the range of potential operational and conduct risk issues relevant to the relationship and the product being underwritten. It is also important that this analysis is recorded and escalated to appropriate levels of management. Where the data analysis indicates an issue, the firm should be able to demonstrate the steps taken to remedy the issue. Firms should resolve serious or repeat breaches as a matter of urgency and escalate them to a senior level.

It is also important that the type and range of MI collected is reviewed periodically to ensure that it continues to provide the firm with the right information and allows the effective monitoring of the operational risk and conduct risk involved. It should take into consideration any changes to the strategy, as outlined in Section 3, and any amendments to the Coverholder authority. Any changes to the product design should also prompt a review of the conduct MI to be collected in order to ensure that it remains relevant and appropriate.

Management information requested may include, but is not limited to:

- Premium income against the GPI limit on the binding authority
- Aggregate exposure reports, providing information to monitor the risks in a particular territory or zone
- Compliance with limits and conditions
- Ensuring the Coverholder is only writing business in the territories for which it is approved
- The Coverholder's, TPA's or outsourcing partner's handling of claims which might include:
    - Accuracy of reserve recommendations
    - Pursuit of recoveries (where appropriate)
    - Timeliness of reporting, reserving, investigations and settlement of claims
    - Frequency and volume of claims
    - Frequency and volume of claims repudiations
    - Repudiation reasons and root cause analysis
    - Selection, monitoring and management of third party experts
    - Coverage analysis
    - Quality of customer (i.e. policyholder) service
    - Breaches of terms of delegation contract
- Rating adequacy
- 'Earned to incurred' reports, providing details of the Coverholder's profitability
- Claims fund reports, providing details of all payments made to and from the claims fund
- Information in respect of the Coverholder's, TPA's or outsourcing partner's handling of complaints which might include:
    - Timeliness of reporting, investigations and settlement of complaints
    - Frequency and volume of complaints
    - Complaints reasons and upheld rates
    - Root cause analysis of complaints
    - Quality of customer (i.e. policyholder) service
    - Breaches of terms of delegation contract
- Point of sale metrics (Advised/Non-advised)
- Method of sale (telephone/distance/face to face)
- Identifier for individual who made the sale
- New business/renewal levels
- Total price paid by customer
- Cancellation volumes and frequency
- Cancellation reasons and root cause analysis
- Other reports to show the Coverholder is keeping to the required service standards

Credit Control

The insurer will need to monitor the performance of the Coverholder with respect to meeting terms of

trade and collection of premiums. This may take the form of:

- Reviewing an aged debt report on a regular basis
- Exception reporting showing cases where terms of trade were exceeded and by how much, per risk written, class of business and territory
- Reviewing an unallocated cash report on a regular basis (this can also be covered as part of the audit conducted)
- Reviewing reinsurance recoveries (where appropriate)

As mentioned in section 5.2 'Insurance Monies', it is essential that the Coverholder understands that insurance monies are held on behalf of underwriters and is held in a separate insurance monies account, separate to their own business accounts. Many jurisdictions require that this separate account must be a trust account. Even where this is not required, the use of trust accounts is strongly recommended. This is important to protect policyholders' funds if the Coverholder becomes insolvent.

Underwriting Performance Reviews

This will encompass the above and could include an underwriting visit where full authority for underwriting has been given or is required by a firm's delegated authority strategy and oversight. The performance reviews should:

- Be conducted at binding authority, Coverholder and class of business levels
- Include a review of the reserves, reinsurance purchased and IBNR
- Provide any analysis as conducted by the actuarial teams, usually at insurer level
- Include an analysis of broker commissions

The ultimate aim is to monitor the Coverholder's performance against service standards and assess profitability of the binding authority against plan and budget

The outcome of such performance monitoring should be reported to the delegated authority committee and Board on a regular basis.

7.4 Post Approval Changes

Proposed changes that pertain to any significant or material aspect of the agreed delegated authority, including any of the criteria assessed in granting the authority (whether proposed by the insurer, Coverholder, TPA or outsourcing partner), should instigate appropriate reassessment of the agreement to ensure that it remains consistent with the firm's strategy, objectives and intended customer outcomes.

Changes that are likely to require consideration include, but are not limited to:

- Coverholder details or circumstances
- The terms of the delegated authority
- The product
- The intended target market
- The distribution framework
- Any relevant legislation or regulation, including consideration of competition law and market share rules

7.5 Audits

Insurers should develop, document and implement a policy that governs their approach to the use of independent (internal or external) audit of entities to which they delegate authority. Firms should outline a clear framework or risk tolerance in respect of the audit outputs and findings so that any response can be prioritised appropriately. It is important to note that audit should be considered a third line of defence detective tool and not an alternative to controls such as performing appropriate

due diligence and having in place appropriate standards and monitoring controls around outcomes.

This policy will normally address:

- The frequency of audits based on the insurer's risk assessment of the entity
- The scope for review to be included in the terms of reference for the auditors
- The identification of appropriately skilled auditors able to fulfil the terms of reference
- The agreement, implementation and tracking of recommendations resulting from the audits

Firms could consider that audits are co-ordinated on a co-insurance basis where possible in order to minimise the disruption to Coverholders.

Risk indicators for developing the in-house audit policy

Each insurer will have a set of key indicators to consider when developing their audit policy. Such risk indicators to consider may include, but are not limited to, the following:

- Coverholder estimated premium income in that particular reporting period
- Level of underwriting and claims authority granted under the binding authority
- Coverholder change in circumstances such as change of ownership, management, territory
- The number of binding authority contracts that the Coverholder manages
- The classes of business written under binding authority contracts
- The territories the Coverholder is conducting business in
- Value of outstanding claims
- Loss ratio
- Level of complaints received
- The conduct risk posed by the binding authority
- The sanctions risk
- Financial crime and money laundering risk
- Internal conduct risk rating

An assessment of these key indicators will enable the insurer to ascertain the frequency with which the Coverholder (or TPA) should be audited.

Auditors

Coverholder audits will normally be conducted by third parties selected according to the insurers' internal selection process and based on:

- Coverholder's audit experience (including a consideration of local and market knowledge).
- Market standards
- Auditor availability in the territory concerned
- Whether the auditor's skills and experience match the audit scope
- Price

Whether audits are conducted by internal or external staff there should be a clear rotation policy in place, ensuring the same individual or firm does not audit the same Coverholder too many times in succession. Ideally, no more than three consecutive audits should be conducted by the same individual or firm.

Audit Scope

An appropriate audit scope will be determined by the insurer for each Coverholder audit they arrange, which will be communicated to the auditor in advance of the audit as part of the terms of reference.

Consideration should be given to the areas to be covered such as:

- Underwriting
- Claims (if authority has been delegated)

- Complaints (if authority has been delegated)
- Conduct risk
- Customer outcomes
- Aggregate, risk and premium bordereau analysis
- Documentation
- Accounting and general finance
- Accounting transactions
- Compliance and governance (including conduct risk)
- IT and data security
- Management oversight
- Review of previous recommendations
- Commission consideration / remuneration structure / final price paid by customer

Report and Follow-up Process

Upon completion of the audits, the auditor should document their findings and any recommendations in a formal report to the insurer. The report should be reviewed by appropriate personnel at the insurer and the recommendations agreed before they are communicated to the Coverholder. Recommendations from the Insurer should include who is responsible for the remedial work and whether the recommendations respond to all the points raised.

When a recommendation made by an auditor is not considered necessary by the insurer, a note confirming the decision not to follow up on the recommendation should be kept on file with a clear explanation for the rationale behind the decision also recorded.

There should be an effective tracking and follow-up process to ensure recommendations made as a result of the audit are recorded, implemented and completed to the insurer's satisfaction; including a clear process for escalation when a recommendation is contentious or the resolution of audit recommendations is problematic or not completed in the required timeframe. The process should also record how effective the actions were in mitigating the risks arising from the outsourced relationship.

The Following Market

Where a Coverholder manages a binding authority that is shared by more than one insurer, it is usually the leader's responsibility to arrange audits. The lead should also notify the following market of the date of the planned audit. The following markets can also be invited to participate, including any following Lloyd's markets, although the cost of audits can be shared across all participants on a pro-rata basis. As such, the audit report should be made available to the following market; either distributed by the lead or via the broker involved. The following insurers should also be kept informed of steps being taken to address issues identified during audits.

7.6 Financial Crime

Insurers have a responsibility to check compliance by Coverholders in respect of anti-money laundering legislation, international sanctions and the Bribery Act 2010. This does not devolve Coverholders of their own individual responsibilities under relevant legislation (both international and local).

Specific questions relating to these issues should be included as part of the Coverholder audit process. At a minimum, Coverholders should be able to demonstrate procedures covering the following:

- Recognition and reporting of suspicious transactions/sanctions issues
- Staff training and awareness
- Record keeping

7.7 Complaints

Insurers have a responsibility to monitor and report on complaints and to ensure that all complaints are handled properly. It is therefore important that insurers are confident that their Coverholders are appropriately and adequately recognising and reporting complaints to them on an ongoing basis. Firms must ensure that complaints information is collated and analysed to determine the root cause of complaints and take any necessary action as a result of the complaints received. Firms should take into consideration the findings of the FCA thematic review on complaint handling: TR14/18 Complaint Handling.

7.8 Problem case monitoring

Insurers must have a procedure in place for identifying and monitoring problem cases. Problem cases can arise where there are serious irregularities such as fraud or dishonesty. Such cases will need to be escalated via the firms' internal escalation procedures to the appropriate personnel and handled accordingly.

However, less serious issues can arise with Coverholders, such as erratic reporting or premium settlement, or lack of progress on audit recommendations. Such matters should be identified via exception reports and escalated to an appropriate forum for resolution and monitoring.

Efficient Record Keeping

Insurers are expected to keep adequate records of all their binding authorities. Some of the key records that the insurers should keep or have access to include the following:

- A copy of the Coverholder Application Form
- Relevant up-to-date information relating to the:
    - Business proposed (for example, the underwriting plan)
    - The Coverholder
    - The broker (if any)
- Information relating to the contract of delegation such as:
    - Any rating basis, schedule or guide
    - Details of certificate wording and extra clauses
    - The format of insurance documents
    - Proposals and claims forms
    - Slip copies and any endorsements
- A copy of the current agreed contract of delegation, including any endorsements
- A copy of the agreement with any TPA
- Copies of relevant statistics, premiums and claims reports, MI collected and any other relevant underwriting information
- Details of any complaints, potential litigation or other potential problems
- Copies of any Coverholder audit reports
- Copies of all visit reports

7.9 Conflicts of Interest

Re-assessment of a Coverholder's conflict management arrangements should form part of the ongoing due diligence and audit scope and should be reviewed on a regular basis. They should be provided on request (or via a Coverholder audit) to the lead insurer for its consideration. The review should include consideration of whether there have been any changes to the original assessment of conflicts of interest and where changes have been identified, firms should ensure that they are addressed and appropriately mitigated.

Conflicts of interest are covered in more detail in section 4.3: *Conflicts of Interest and Coverholders and Conflicts of Interest sections.*

SECTION 8 - NON-RENEWAL AND TERMINATION

8.1 Introduction

Insurers should deal with non-renewal or termination of a delegated authority contract in an appropriate manner.

8.2 Non-renewal of binding authorities

When deciding whether to renew a contract of delegation, the insurer should consider the following (in addition to underwriting assessments of the contract):

- The relevant licenses, permits, and errors and omissions insurance held by the Coverholder
- The Coverholder's financial standing
- How the Coverholder has administered and operated the binding authority (including keeping to the required service standards)
- Significant changes to the Coverholder's circumstances
- Other problems or potential issues (for example, arising from any audit or underwriting visits, complaints or potential litigation or regulatory issues)

If a binding authority is not renewed, it is essential that its run-off be closely monitored. Some of the considerations highlighted below for terminated binding authorities will also be relevant for binding authorities which have not been renewed.

Practical implication of non-renewal

Some jurisdictions regulate an insurer's processes for renewing or not renewing an insurance contract. These regulations are particularly common for insurance bought by individual consumers rather than businesses. In such cases, an insurer proposing not to renew a contract of insurance may need to provide a notice of non-renewal in a particular form, giving a specified period of notice before the insurance will end. Failure to do so can mean the contract of insurance automatically renews on its previous terms and conditions.

The Coverholder must handle the non-renewal of such contracts of insurance in line with local law and requirements. The insurer must also consider the effect of such provisions if it has decided not to renew the binding authority. It is important that the broker (if any) and Coverholder be given sufficient notice of any decision not to renew the binding authority. This will give them a reasonable opportunity to handle the non-renewal of individual contracts of insurance correctly. If reasonable notice is not given of the decision not to renew a binding authority, or it is not ensured that the Coverholder handles non-renewal of contracts of insurance correctly, the insurer underwriting the binding authority may be committed to renewing individual contracts of insurance.

Consideration must be given where there is a lead/follow arrangement in the delegated authority agreement. If the firm acts as the lead in the arrangement, depending on the reasons for wishing to terminate the arrangement, consideration must be given as to whether the entire arrangement should also terminate or a replacement lead should be appointed. In this case, it should satisfy itself that the replacement lead is able to act in a lead capacity, has the necessary knowledge, resources and information to undertake such a role and that the following market is notified and agrees to this change. Notice will have to be given to the lead insurer if the firm has adopted a following role.

8.3 Termination of the binding authority contract

The termination of a current binding authority is a significant event. A binding authority is usually only terminated mid-term if there are serious problems with the Coverholder (for example, not meeting licensing or regulatory requirements, issuing insurance documents without insurance cover or where there is fraud or dishonesty).

It is essential that the termination is handled effectively to avoid disproportionate amounts of management time being invested in resolving issues, such as operational and reputational risks for the insurer involved. The binding authority will allow the insurer to cancel the contract. If the insurer does terminate a binding authority, it should follow any notice requirements and any other relevant limitations or conditions specified in the contract of delegation.

Before giving notice

The main considerations to bear in mind before giving notice of termination include the following:

- Identifying who needs to be informed and when. This may include:
  - The relevant broker.
  - The following insurers, any contracted TPAs or outsourcing partners.
  - Any local representative.
  - Coverholder auditors.
  - Relevant regulators, depending on reasons for termination (see Section 9).
- Consideration of how a termination of the agreement may affect the customer and appropriate mitigation processes to avoid customer harm.
- Identifying how the notice should be delivered to the Coverholder, considering the terms outlined in the binding authority.
- Preparing the notice. This is vital because it will set out precisely what the Coverholder is expected to do during the period of notice and once the notice has ended. Particular attention is needed to make sure the Coverholder is clear about how amendments to existing contracts of insurance and new contracts of insurance will be treated.
- Responsibility for any additional costs and expenses incurred by invoking the termination process should be clearly allocated.
- Identifying potential substitute Coverholder run-off providers. These should be identified at an early stage in case it is necessary to transfer the responsibility for run-off away from the Coverholder.
- Consideration of the customer ownership provisions in the agreement (as outlined in table 5.2 A).
- A clearly defined action plan that considers the need for a customer contact process, to ensure that appropriate and relevant information is delivered to the ultimate customer, in a timely manner and establishes who is responsible for any customer contact.
- Consideration of any relevant IP ownership, including but not limited to IT platforms, which could be fundamental to the product distribution and customer contact process.
- Identifying potential TUPE obligations.
- Considering whether it is necessary to put a representative of insurers in the Coverholder's offices to supervise the Coverholder during the notice period.
- Identifying who to speak to at the Coverholder’s offices to explain the reasons for the cancellation and what will be happening. Wherever possible, the insurer will want to keep a good working relationship with the Coverholder.
- Requiring the Coverholder to return any unused insurance documents or other materials they have in connection with the binding authority and which might be used as evidence of insurance and which bear the name of, or refer to the insurer. If the Coverholder prints certificates, the insurer should instruct them not to print any further certificates.
- Establish who will carry out the handling of claims and/or complaints after the termination of the contract, having carried out all necessary due diligence and prepared the necessary contractual and process documentation if a new TPA or outsourcing partner is to be appointed.

Giving notice

Under the terms of the IUA model binding authority wording, working notice needs to be in writing and delivered to the Coverholder with a copy provided to the broker (if there is one).

After giving notice

After the notice has been given, the insurer should:

- Closely monitor the contracts of insurance which the Coverholder enters into during the notice period and make sure the Coverholder does not enter into any contracts of insurance after the notice period ends
- Visit the Coverholder or send Coverholder auditors to make sure the run-off is being handled effectively
- Ask for appropriate reports from the Coverholder, TPA or outsourcing partner in order to monitor the handling of the run-off (paying particular attention to customer service levels, claims handling and reporting of any difficulties or complaints)
- Make sure the Coverholder, TPA or outsourcing partner has sufficient funds to pay claims
- Satisfy itself that the Coverholder's, TPA's or outsourcing partner's financial position remains adequate
- Satisfy itself that the customer is not being adversely affected
- Satisfy itself that the Coverholder, TPA or outsourcing partner has adequate human resources to handle the run-off
- Make sure the insurer has access to all key documents relevant to the run-off (for example, claims files)
- Ensure adherence to data protection retention and deletion procedures and requirements

In some circumstances where a binding authority has been terminated or not renewed, it may not be possible or appropriate for the Coverholder, TPA or outsourcing partner to handle the run-off. This may be for a variety of reasons.

If the run-off responsibilities are transferred to another party, the insurer will need to make sure of the following:

- Appropriate due diligence has been undertaken in respect of the other party
- Appropriate information is given to customers in a relevant manner to explain the position and give details of the replacement contact point for the policy
- The terms of the contract or binding authority have been agreed with the other party before any transfer is undertaken
- All relevant insurance and claims documents are transferred
- A suitably experienced party is appointed to handle the run-off and has clearly defined responsibilities and service standards
- Appropriate processes are in place to avoid customer harm
- The reputation of the insurer is protected and if the insurer deems the circumstances require, any local regulator is properly briefed about the transfer

SECTION 9 – NOTIFICATION CONSIDERATIONS

9.1 Notification Considerations

Insurers should follow the appropriate internal escalation procedures when any serious concern or issue arises. Consideration should also be given to notifying any relevant regulatory authorities of those concerns that arise in their dealings with Coverholders, TPAs or outsourcing partners. A 'serious concern or issue' would be one which, if substantiated and uncorrected, would:

- Result in the Compliance Officer or Underwriter of that insurer deciding to cancel the contract or commence legal action against the Coverholder, TPA or outsourcing partner; or otherwise indicate that the Coverholder, TPA or outsourcing partner may no longer be suitable to be approved

Situations where the relevant regulatory authority would likely expect to be informed of issues include where the Coverholder, TPA or outsourcing partner has:

- Become insolvent/bankrupt
- Committed (or may have committed) a criminal offence or acted fraudulently (this includes principal officers)
- Written outside the terms of the binding authority
- Operated outside its authority
- Failed to pass on funds received from policyholders
- Behaved in a way that risks damaging the insurers licences or reputation
- Systems that may not be 'fit for purpose' (not sufficiently robust to efficiently administer or report on the business bound)
- Suffered a data breach

This list is not exhaustive and if in doubt the insurer should consider notifying the appropriate regulator of the concern.

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