

MARKET BULLETIN

REF: Y4739

Title	Coverholder approval, restricted coverholders and Consumer Product Binding Authorities
Purpose	To inform the market of: <ul style="list-style-type: none"> • proposed changes to the way in which coverholders are approved, including the removal of the restricted coverholder status; and • enhanced requirements for the oversight of consumer business written through binding authorities;
Type	Event
From	Peter Montanaro Head, Delegated Authorities Team Performance Management Directorate
Date	8 November 2013
Deadline	As set out in bulletin
Related links	Intermediaries Byelaw ; Requirements made under the Intermediaries Byelaw ; Delegated Underwriting Code of Practice

Lloyd's operates a coverholder approval process to ensure all coverholders remain suitable to be a coverholder at Lloyd's. The present Lloyd's framework for coverholder approval was put in place in 2004. Since then, in addition to changes to market practice, there have been significant changes to the regulation of insurance both in the UK and internationally. In particular there has been an increased focus on the selling of financial products to consumers, including insurance products.

To reflect these changes, and having worked closely with market working groups, Lloyd's has developed proposals to enhance Lloyd's risk management processes as they apply to business bound by coverholders where there is consumer business. This will involve -

- The removal of the restricted coverholder category of coverholders. Instead, Lloyd's proposes to adopt a new tiered approach to coverholder approval. While coverholders with full underwriting authority will continue to be subject to the full coverholder approval process, coverholders with reduced levels of authority will be subject to an approval process that reflects their level of underwriting authority.

- Managing agents writing Consumer Product Binding Authorities (as defined further below) will be expected to clearly evidence their due diligence of the conduct risk.
- The introduction of a new minimum standard that addresses conduct risk.

A market presentation will be held on 19 November 2013 to provide managing agents, brokers and coverholders with more information and the opportunity to provide feedback or ask questions. Details of the market presentation and how to provide feedback in writing are set out at the end of this bulletin.

The current Lloyd's coverholder approval arrangements

Lloyd's current requirements are as set out in the [Intermediaries Byelaw](#) and the [requirements made under that Byelaw](#). In summary, all Lloyd's coverholders are either:

- (a) fully approved coverholders, which means that they will have needed to satisfy Lloyd's they are suitable to be approved and in this regard Lloyd's will have assessed the coverholder against a number of published criteria. There are currently 3020 approved coverholders in the UK and worldwide; or
- (b) restricted coverholders, which means that whilst the coverholder will have been registered by a managing agent it will not have been approved or subject to any due diligence by Lloyd's. There are currently 2904 restricted coverholders in the UK. The key features of these coverholders are:

- No underwriting discretion
- Retail-facing only
- Limited to specific personal lines classes of business
- Domiciled in the UK and only underwriting UK risks

This approach as presently adopted by Lloyd's reflects the fact that coverholders with significant levels of underwriting authority need to demonstrate a higher level of underwriting expertise and should therefore be subject to a more rigorous approval process. Where coverholders write UK business only and do not have underwriting authority Lloyd's has been satisfied that registration of the coverholder is sufficient without a formal Lloyd's approval process.

Lloyd's, however, has already begun to adopt a more risk based approach to approval and this strict dual categorisation of coverholders is not helpful in that regard. For instance some approved coverholders are currently subject to the full approval process but have only limited levels of underwriting authority. In contrast restricted coverholders are not at present subject to an approval process by Lloyd's, yet a significant amount of restricted coverholder business is consumer business which requires a high level of regulatory compliance. Lloyd's presently has very little information on these coverholders and no information as to the binding authorities they hold. Lloyd's therefore has very limited assurances as to the way this business is written.

The proposed changes

1. Updated categorisation of coverholder approval

Lloyd’s therefore proposes to replace the current approved coverholder and restricted coverholder distinction so that going forward all coverholders will be approved by Lloyd’s (and the restricted coverholder category will be removed). This will necessitate coverholders that under the current rules would be restricted coverholders having to go through a more rigorous approval process. However the approval process will be tailored to the level of underwriting authority given to the coverholder. Coverholders with full underwriting discretion will continue to be subject to the current full application process. Where coverholders have reduced underwriting authority the information required will be tailored to the level of underwriting authority they are given. For instance, a “no discretion” coverholder will not need to provide information regarding its underwriting capabilities.

The relevant authority levels will be -

Level of Authority	Definition
Full Authority	The coverholder may be given full discretion to set rates or given minimum rates from which the coverholder has discretion to increase rates without restriction or referral.
Pre-determined rates	The coverholder may only be given underwriting authority via a rating matrix or range within which the rates can be established. The coverholder has authority to exercise minimum underwriting discretion within agreed parameters, for example within a percentage of the standard premium.
No discretion	The coverholder may only be given underwriting authority via a comprehensive rating matrix. These arrangements must not give the coverholder discretion in calculating the premium or making adjustments to it, other than minimal rounding up.
Prior submit	Each risk must be referred from the coverholder to the lead underwriter before being bound.

1.1 Implications for new restricted coverholders

In the future such coverholders will need to be approved by Lloyd’s and a coverholder application on ATLAS will be required. By requiring an ATLAS application for these coverholders Lloyd’s can now ensure it has a suitable level of information and oversight. As these coverholders will fall within the new “no discretion” or “prior submit” category, the approval process will reflect the fact that the business written presents a lower underwriting risk.

To give effect to this it is proposed that the references to restricted coverholders will be removed from the Intermediaries Byelaw. This proposal is subject to consideration and approval by Council.

1.2 Implications for existing restricted coverholders

All existing restricted coverholders will be grandfathered onto the register of approved coverholders and their details included on ATLAS. This will ensure a record of these coverholders is held centrally. In addition, all branches of restricted coverholders which are engaged in Lloyd's coverholder activities will have to be separately registered with Lloyd's (via ATLAS).

In order to ensure all current restricted coverholders are grandfathered a simple data collection exercise will be carried out at the beginning of 2014. This will involve Lloyd's sending each managing agent a list of their existing restricted coverholders as recorded by Lloyd's and presently shown on the restricted coverholders website. Managing agents will be asked to provide confirmation of which relationships remain current and confirmation of any additional relationships required. Brokers will also be sent a list of restricted coverholders to confirm which coverholders they will require relationships with on ATLAS.

Going forward the previously restricted, but now approved, coverholders will be subject to the same ongoing oversight as other approved coverholders. This includes ATLAS details being kept up-to-date, annual compliance being completed, audits being conducted in line with the managing agent's audit policy, binding authorities being registered on BAR and adherence to all other requirements set out in the [Delegated Underwriting Code of Practice](#). All grandfathered restricted coverholders will be expected to sign the Lloyd's Coverholder Undertaking within a year of being put onto ATLAS.

Further details on the grandfathering processes will be sent to managing agents, Lloyd's brokers and relevant coverholders in due course.

2. **A new approach to Consumer Product Binding Authorities**

In reviewing its oversight of coverholders, Lloyd's has considered the standards and procedures that are appropriate to manage "conduct risk". By conduct risk we mean the risk that behaviours or processes result in a poor outcome for policyholders. In particular we have focussed on the conduct risk where coverholders are permitted to write consumer business.

Addressing this is important and timely given the increased regulatory emphasis on the selling of financial products to consumers, including insurance products. Any failure to manage properly conduct risk may lead to managing agents or their coverholders facing regulatory intervention (including substantial fines). This is in addition to the complaints that can arise, contractual disputes and adverse publicity. In addition to ensuring that policyholders are treated fairly, it is therefore also in the interests of both managing agents and coverholders to ensure that this risk area is being properly managed.

Lloyd's is therefore proposing that managing agents should be able to evidence appropriate due diligence in respect of binding authorities which are classified as Consumer Product Binding Authorities (CPB).

2.1 What is a Consumer Product Binding Authority (CPB)?

A CPB is a binding authority under which a consumer product is distributed by a coverholder. This means that the end customer is a consumer regardless of whether the coverholder is distributing the product directly to the consumer or through a producing broker. For these purposes, Lloyd's considers the following to be consumers:

- Private individuals
- Small businesses, commonly referred to as micro-enterprises, or other small non-business organisations
- Any other entity that would be considered a consumer by the relevant regulatory authority in the local territory

2.2 Due diligence of CPBs

Where managing agents are proposing to allow coverholders to write under a CPB, Lloyd's will expect to be provided with evidence that the managing agent has carried out an appropriate level of due diligence to ensure conduct risk is adequately addressed for that binding authority. In practice this means managing agents will have to assess all coverholders for each CPB entered into to ensure conduct risk is assessed for all their consumer business worldwide.

To assist managing agents evidence their assessment of conduct risk Lloyd's has prepared a model CPB Questionnaire (Appendix 1) to be completed each time a CPB is entered into with a coverholder. This questionnaire provides a template to allow a managing agent to evidence its consideration of conduct issues. The CPB Questionnaire is intended for completion by managing agents rather than the coverholder (although the managing agent may wish to discuss the questionnaire with the coverholder or broker). Consideration may also need to be given to any relevant local consumer requirements for overseas business.

The use of this questionnaire is not mandatory and managing agents may choose to use or develop their own assessment process. Any alternative process should as a minimum address the same risk areas as the model questionnaire and must be capable of evidencing how the managing agent has satisfied itself that the coverholder meets a satisfactory conduct standard.

Managing agents should ensure that they maintain up-to-date evidence of their assessments for all their coverholders' CPBs. These should be updated ideally annually. The questionnaire (or the managing agent's own equivalent process) must be completed for all CPBs irrespective of the level of underwriting authority given to the coverholder. This includes coverholders who are approved under the new "no discretion" or "prior submit" category.

2.3 Provision of the questionnaire to Lloyd's

Lloyd's may request a copy of a managing agent's questionnaire for a CPB. Lloyd's will also always expect to be provided with a copy of the questionnaire (or equivalent) for all new coverholder applications and class of business requests which relate to coverholders that will operate under CPBs. The questionnaire can be attached to the ATLAS application or to the letter of support.

2.4 Introduction of the new process

Lloyd's proposes to pilot CPB Questionnaires from January 2014 during which time Lloyd's will welcome feedback and comments. It is intended that the new arrangements will be made mandatory from the middle of 2014.

3. **A new minimum standard**

A fifth minimum standard setting out the expected standard for the management of conduct risk in delegated underwriting has been drafted and is currently being reviewed as part of the Minimum Standards consultation process. It will be shared with the whole market for feedback as part of this process in due course.

4. **Further information and feedback**

4.1 Feedback and questions

Some of the changes Lloyd's proposes to implement will be subject to consideration by the Council of Lloyd's in due course including to make the necessary changes to Lloyd's Byelaws. Lloyd's would welcome any feedback on the proposals ahead of the proposed byelaw changes being put to the Council of Lloyd's.

Feedback or questions can be sent to Gabriella Barker by email at Gabriella.Barker@lloyds.com.

4.2 Market Meeting

Lloyd's Delegated Authority Team will be holding a market meeting to discuss the proposals from 9.45am – 12pm on Tuesday 19th November with tea and coffee from 9.20am. This will give the market the opportunity to hear Lloyd's Delegated Authorities team talk about the changes outlined in this bulletin and to ask questions. If you would like to attend please RSVP to Annabelle.Mayers@lloyds.com by 12 November 2013.

Appendix 1: Consumer Product Binding Authority (CPB) Questionnaire

Satisfactory completion of this questionnaire is the responsibility of a Managing Agent. Should you require further guidance on assessing the definition and requirements of a CPB please refer to Lloyd’s Delegated Authorities team.

Lloyd’s requires this form, or an equivalent document, to be completed for all new Coverholder applications and new class of business applications submitted to Lloyd’s for approval that relate to CPBs. The completed questionnaire must be attached to the Atlas application or submitted as an attachment to the Managing Agent letter of support.

For a new CPB where an application to Lloyd's is not required or for renewals of a CPB, Lloyd's recommends Managing Agents utilise the form to ensure they maintain the appropriate oversight of consumer products. This is not mandatory. However in the absence of the form Lloyd’s expects Managing Agents to be able to demonstrate that they have in place equivalent arrangements to assess and manage the relevant risk areas.

Coverholder Name:			
PIN:			
Syndicate:		Broker:	
Lloyd’s Class(es) of Business:			

1. Product Design and Suitability
a. How have you satisfied yourself that the product offers suitable value and cover for the intended consumer?
b. Where a new product is proposed, how have you satisfied yourself that: <ul style="list-style-type: none"> • You know and record which stakeholder is responsible for the initial product design • The product has been appropriately screened to determine whether it offers suitable value for the intended customer • The likelihood of a claim under the proposed product and the likely frequency has been assessed and this analysis been considered and reflected in initial pricing • Where a product is intended to be offered as a package or add-on it is reasonable to expect the customer to know the cover exists and to remember this at the point a possible claim could arise.

2. Financial Promotions	
a. Will any financial promotions be launched for the product(s) written under this binding authority?	Y / N
<i>If 'No' go to question 3</i>	
b. If yes, how have you satisfied yourself that: <ul style="list-style-type: none"> • Financial promotions are clear, fair and not misleading and target the right customer • Benefits are accurately reflected and relevant risks are sufficiently highlighted • Queries and complaints arising from financial promotions are monitored and action taken where necessary. 	

3. Product Distribution and Information	
a. How have you satisfied yourself that the product distribution channel is suitable, having given consideration to: <ul style="list-style-type: none"> • Which stakeholders are marketing and selling to the customer and their level of understanding of the product • What is done to ensure the customer fully understands the product and that such discussions and communications are recorded appropriately • How sales are monitored to ensure the product is sold to the intended customers • The intended volume of customers and that the relevant stakeholders have appropriate resources • Staff incentives and reward schemes that could conflict with the interest of the customer 	
b. How have you satisfied yourself that information provided to the customer is clear, fair and not misleading, having given consideration to: <ul style="list-style-type: none"> • Whether the customer receives any advice and if so the competence of those giving advice and the appropriateness of the advice itself • The content and frequency of information given to the customer throughout the duration of the relationship • Technical terminology and whether such terminology is clearly explained • The process for providing information in a timely and efficient manner should it be sought by the customer 	

4. Barriers
<p>a. How have you satisfied yourself that the customer is not at risk of facing barriers should they wish to cease, amend or switch products, having given consideration to:</p> <ul style="list-style-type: none"> • Whether there are any high or disproportionate penalties for such actions • Whether there are any excessive complications or administration • Whether any conditions apply with negative consequences for the customer, such as long exclusion periods during which a claim cannot be made

5. Claims
<p>a. Which stakeholder will be responsible for handling claims under this binding authority?</p>
<p>b. Where a stakeholder other than yourself will be responsible for claims handling, how have you satisfied yourself that service issues and claims are processed, responded to and settled in a timely and fair manner giving consideration to:</p> <ul style="list-style-type: none"> • Whether reasonable guidance is given to the customer with regards to how to make a claim • Whether the stakeholder has authority to reject a claim and if so, how you ensure rejections are reasonable and that the reason for rejection is appropriately recorded • Whether claims are settled promptly and how this is monitored
<p>c. How have you satisfied yourself that claims will be handled in accordance with Lloyd's requirements?</p>

6. Complaints
<p>a. Which stakeholder will be responsible for handling complaints under this binding authority?</p>

<p>b. Where a stakeholder other than yourself is responsible for handling complaints, how have you satisfied yourself that complaints are dealt with in a reasonable and prompt way giving consideration to:</p> <ul style="list-style-type: none"> • The process for logging and handling complaints (including acknowledging complaints) • The Coverholders/stakeholders understanding of what constitutes a complaint • What information is captured and its reporting to Underwriters in a timely manner • In handling complaints any recurring or systemic problems are identified and remedied.
<p>c. How have you satisfied yourself that complaints will be handled in accordance with Lloyd's requirements?</p>

<p>7. Fair Treatment of Customers</p>
<p>a. How have you satisfied yourself that the Coverholder is complying with their obligations to ensure the fair treatment of their customers, giving consideration to:</p> <ul style="list-style-type: none"> • How the Coverholder engages, motivates and trains staff on the fair treatment of customers and how they monitor staff understanding • How issues are recorded and managed.

<p>8. Reporting requirements</p>
<p>a. How have you satisfied yourself that you have access to the data required in order to appropriately monitor that the product continues to be suitable for the intended customer and that this data will be adequate for relevant regulatory reporting requirements?</p>

9. Compliance with international conduct requirements (where applicable)

- a. Where the binder will provide cover to consumers in territories outside the United Kingdom, how have you satisfied yourself that the coverholder is aware of local conduct requirements and has appropriate controls in place to ensure compliance with these having given consideration to:
- Whether the coverholder has appropriate infrastructure in place to deal with volumes of enquiries/servicing requests or complaints in respect of the cover issued to overseas consumers
 - Whether the Coverholders is able to meet any local language requirements, where applicable.