

Guernsey Financial Services Commission

**Feedback and Final Consultation on
Professional Indemnity Insurance for Insurance
Intermediaries and Insurance Managers**

Issued 10 June 2022

Contents

| | |
|---|---|
| Background | 3 |
| Professional Indemnity Insurance..... | 4 |
| What was the general message in the feedback? | 4 |
| What is the Commission going to do next?..... | 4 |
| Specific Feedback and Changes..... | 4 |

Background

On the 8 December 2021 the Commission published a consultation paper (“CP”) on professional indemnity insurance (“PII”). The Consultation period ran for 9 weeks until 14 February 2022.

There was a healthy response to the CP which saw 10 responses. Four of the respondents were intermediaries (two long-term, one combined long-term and general, and one general), four were insurance managers, one was an insurer and one was an industry consultant.

The CP is available on the [Consultation Hub](#).

Professional Indemnity Insurance

What was the general message in the feedback?

The Commission published the CP to seek stakeholders' views on proposed changes to the rules in respect of the maintenance of PII. The protection of the public against financial loss due to dishonesty, incompetence or malpractice by persons carrying on finance business is a statutory function of the Commission. One of the ways the Commission carries out this function is to require that certain financial services businesses maintain PII. The Commission also considers it desirable for customers to have access to high quality insurance advice.

The purpose of the CP was to seek stakeholders' views on changes to the current PII rules to modernise them whilst ensuring both that customers are able to access high quality advice, and that they are also protected in the event of losses from poor quality advice.

In general most of the respondents broadly supported the proposals in the CP. The range of the responses reflected the industry sectors and the relative size of the firms, and for some proposals there were equal numbers agreeing and disagreeing with them. A number of the respondents reported that some of the proposed changes would be particularly onerous in the current challenging PII market and the Commission is not proposing to take these forward at this time.

What is the Commission going to do next?

Alongside this feedback statement the Commission has issued a final draft of the relevant amended rules wording, taking into account comments received during the consultation. A final eight-week consultation period is being offered to provide an opportunity to identify any "fatal flaws" in the draft amended rules, after which amendments will be formally adopted.

The draft rules are attached for fatal flaw comments by 5 August 2022

A summary of the responses received to each question in the CP, together with the Commission's feedback, are presented below.

Specific Feedback and Changes

1. £10,000,000 cap on the annual aggregate level of PII cover required

Respondents were generally supportive. A number noted that their turnover was not high enough for them to be affected. Two respondents commented that it was more important that a firm buy sufficient cover for the risks of the business and any cap would inevitably be somewhat arbitrary. One respondent questioned the benefit of a cap for clients. Several respondents felt a limit of £10,000,000 would make it easier to obtain cover.

2. Minimum cover for each and every loss increased to £1,000,000

There was a mixed response to increasing the individual loss limit to £1,000,000: some respondents supported it as a claim could easily exceed £250,000, particularly when legal fees are included. Other respondents felt that any increase would make it harder to buy

cover (although the research carried out before the CP indicated that all the firms in the survey currently bought £1,000,000 or more).

One correspondent felt that the each and every loss limit should be variable based upon the size of the business. The Commission recognises that this approach may appear more proportionate, however industry claims data does not show a strong correlation between firm size and claim size. Using size or other variables would also be difficult to manage and monitor.

Two respondents noted that each and every claim's limits were not standard across the market and may make obtaining cover harder. The Commission does not require firms to maintain limits for each and every claim. The purpose of the each and every loss limit section within the Rules is to ensure that firms, having arranged an appropriate amount of cover in the aggregate, do not then limit each and every loss within the aggregate to a small amount thus negating the benefit of cover. The Commission's preference is for firms to buy cover which has no individual claims' limits. Where firms choose to put in place individual limits, whether to increase availability of cover or reduce cost, then those limits must not be less than £1,000,000.

3. Firms are required to maintain PII cover which is consistent with size and nature of its business, and document that process

This proposal was agreed by all respondents, however there was some concern about how the Commission would determine whether the cover was consistent with the size and nature of a firm's business, particularly if reviewing the process with the benefit of hindsight.

The CP includes the proposal that firms must document the process for determining the level of PII that is appropriate for the size and nature of the business. As with any engagement following a supervisory event, a licensee's ability to demonstrate the suitability of its actions with thorough, contemporaneous documentation will assist it in demonstrating that its actions were appropriate.

4. The introduction of minimum policy terms and conditions

a. Cover for negligence, errors or omissions by the licensee or its employees

There were no comments.

b. Cover for any liability for the dishonest or fraudulent acts of employees which may fall on the licensee

One respondent commented that dishonest or fraudulent acts of employees may be covered by a policy other than professional indemnity insurance. The Commission has amended the rules to make it clear that this cover may be provided by a policy other than professional indemnity subject to it meeting the other requirements of the rules.

c. Cover for liabilities of its employees who, in the course of their duties to the licensee, perform functions in their own names

One respondent expressed concern about whether the proposed rules would make firms liable for the unauthorised actions of their employees. The purpose of this section is to

ensure that members of staff who take a role as part of their employment with the licensee but not in the licensee's name, for example being director of a charity the licensee is associated with, would also be covered for the advice given in that position. The Commission considers it important that where a third party might reasonably assume the employee is representing the licensee that appropriate cover is in place if that advice is relied upon.

d. Cover for liabilities which the licensee might incur in any jurisdiction in which it carries on business

This proposal was generally accepted although one respondent asked for clarification of the term "carries on business" in a jurisdiction. The Commission's preference is that all firms buy cover on a worldwide basis as clients may travel or move. The Commission recognises, however, that this may not always be possible. As a minimum the Commission expects firms to have coverage for every territory in which they could reasonably expect to be subject to action in the event of negligence. For example, a general insurance broker arranging household insurance in Guernsey could reasonably expect to be held liable for negligence in Guernsey; an IFA advising a complex financial structure with connections to a large number of different jurisdictions should maintain a policy that includes all those jurisdictions.

e. Ombudsman awards

There were no comments.

f. Legal defence costs

Please see below.

g. Defence costs must not contribute to the aggregate limit

The Commission is concerned that legal costs are forming an increasingly large share of total claims costs. In the event that there is a large claim or series of smaller claims the available cover could be used up paying legal fees and there may not be sufficient funds left to indemnifying the clients who have suffered the loss.

The Commission's proposal to protect the clients' interests was to ensure that legal costs did not count towards the aggregate. This a requirement in some jurisdictions. However, the Commission has taken onboard the feedback from respondents that this cover is not universally available and would potentially limit even further the number of underwriters prepared to write this risk for Guernsey firms. The Commission is therefore not pursuing this proposal at this time.

h. Retroactive date from the date the firm was licensed

One respondent commented that underwriters may limit the retroactive date where the firm has changed in nature over the years and coverage has changed. The Commission considers that all firms should endeavour to secure cover from the date they are licensed to ensure that all clients are protected equally, however the Commission will retain the

ability to waive or amend this requirement in the event that it would be disproportionate and clients are not put at a materially increased risk.

5. Fee income

The Insurance Intermediaries Rules and the Insurance Managers Rules require that licensees maintain cover of “three times fee income”. The Consultation Paper did not consult on any changes to these requirements, however one of the purposes of the proposed changes is to introduce more consistency between the rules for different sectors in the financial services industry in Guernsey. The consultation on rules for the investment and fiduciary sectors is suggesting a clarification of their wording and it is proposed that a similar wording be used within the Insurance Intermediaries Rules and the Insurance Managers Rules.

It is proposed that the requirement for licensees going forward will be to maintain three times income from regulated activities, with an expectation that firms will consider arranging additional insurance if unregulated activities form a significant part of the firm’s business or is at greater risk of generating relevant insurance claims. As most firms in the insurance intermediary and manager sectors do not carry out any material unregulated activities this is not expected to have a significant impact on industry.