

# Draft amended Insurance Managers and Insurance Intermediaries PII Rules for fatal flaws comments

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## Results updated 2 Sep 2022

Comments on the draft amended Insurance Intermediary Rules and Insurance Managers Rules (together “the Rules”) were received from three respondents. Some minor changes have been made to the final rules to ensure consistency of drafting but there has been no change to the substance of the requirements.

The Commission has now issued the amendments which give effect to the amended rules. The amending instruments include transitional provisions concerning insurance arrangements which enable licensees to make any necessary changes to comply with the amended rules at the point at which their insurance renewal falls due. The rules and guidance have been updated. Consolidated versions of the rules are available on the Commission’s website.

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## Overview

## Background

In our December 2021 [Consultation Paper on Professional Indemnity Insurance](#) we asked for feedback on the proposed changes to requirements concerning professional indemnity insurance (“PII”) for insurance managers and insurance intermediaries.

A feedback statement on the CP can be found at the link below. Alongside the feedback statement the Commission has issued final drafts 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.

Excerpts of the draft amended Insurance Managers Rules and Guidance, 2021 and the draft amended Insurance Intermediaries can be found below.

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## Related

- ➔ [Feedback Statement to PII CP - Insurance Managers and Insurance Intermediaries](#)
- ➔ [Excerpt from draft amended Insurance Manager Rules](#)
- ➔ [Excerpt from draft amended Insurance Intermediaries Rules](#)

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## Audiences

Insurance Managers   Insurance Intermediaries

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Guernsey Financial Services Commission

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

Issued 10 June 2022

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## 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.

Excerpt from the Insurance Managers Rules

PART 7 – CONDUCT OF BUSINESS

7.5 Professional indemnity insurance

7.5.1 A licensee must maintain adequate insurance at all times, commensurate with the size and nature of its business activities. Such cover must include professional indemnity insurance and insurance against employee dishonesty or fraud as required by this section.

7.5.2 Minimum requirement

7.5(1) A licensee must maintain the minimum cover as laid out in subsection (2). The board is responsible for ensuring that the insurance arrangements for the licensee are adequate. Where the licensee concludes that amount of insurance required for the size and nature of its business is greater than the maximum amount in (2)(b) then the amount of cover the licensee is required to maintain is the higher amount.

(1)(2) Subject to subsection (3) Every licensee must maintain professional indemnity insurance and employee dishonesty or fraud insurance with the following minimum limits –

(a) on the basis of each and every loss, cover of at least £250,000~~£1,000,000~~; and

(b) on an annual basis, £1,000,000 or three times fee income from regulated activities income, whichever is the greater.

Guidance

The income from regulated activities should be based on the latest audited financial statements at the time of the relevant insurance renewal.

For the avoidance of doubt, insurance cover based on a prior year's audited financial statements does not need to be amended before the next annual renewal following the release of the following year's financial statements. However, a licensee is expected to consider whether additional cover should be arranged with immediate effect in the event that the audited financial statements show a material increase in regulatory income.

(3) Where the licensee also carries out unregulated activities, the licensee must consider whether the minimum indemnity limit of its insurance policies and scope of the insurance cover are appropriate for its businesses as a whole, taking into account possible claims that may also arise from unregulated businesses.

(4) Notwithstanding Rule 7.5.2(2), above, a licensee is not required to have aggregate insurance cover exceeding £10,000,000 provided that the Board of the licensee has considered and decided that such level of cover is appropriate and sufficient for its business. The licensee must be able to evidence the Board's assessment if requested by the Commission.

Guidance

The consideration by a licensee of its insurance requirements should be clearly documented at local board or senior management level to demonstrate how the decision was made. The Commission expects all licensees, whether or not they are part of organisations with offices elsewhere, to consider the insurance requirements for the entities in the Bailiwick of Guernsey.

Where a local operation is part of a group and the local board or management do not consider the cover available to the Guernsey licensee to be adequate the Commission expects the board or management to make arrangements to maintain appropriate cover. This may include purchasing a separate policy for the local operation.

~~(b)~~

(5) Where the deductible or excess exceeds £20,000 on the basis of each and every loss, the minimum capital requirement will increase to 125% of the deductible or excess.

~~(2)~~

- (6) A licensee must maintain at all times cover for:
- (a) negligence, errors or omissions by the licensee or its employees;
  - (b) any liability for the dishonest or fraudulent acts of employees which may fall on the licensee;
  - (c) liabilities of its employees who, in the course of their duties to the licensee, perform functions in their own names;
  - (d) liabilities which the licensee might incur in any jurisdiction in which it should reasonably foresee that it may be held liable for damages and costs;
  - (e) where relevant, ombudsman awards; and
  - (f) legal defence costs.
- (7) The retroactive date for the insurance arrangements in this section must be the date the licensee was licensed by the Commission.

7.5.27.5.3 Notifications to the insurer

- (1) A licensee must –
- (a) when applying for cover, notify his professional indemnity insurer, through their professional indemnity insurance broker, of all material facts, which must include –
    - (i) the details of any condition imposed on the licensee under section 7 of the Law;
    - (ii) the revocation of the licensee's licence under section 9 of the Law;
    - (iii) any regulatory penalty taken by the Commission against the licensee, or any of its directors or employees, under the Financial Services Commission (Bailiwick of Guernsey) Law, 1987<sup>8</sup> ("the FSC Law") or any of the Regulatory Laws;

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<sup>8</sup> Order In Council No. XXX of 1987.

- (iv) any prohibition order made against the licensee, or any of its directors or employees;
  - (v) any criminal proceedings commenced against the licensee, or any of its directors or employees; and
  - (vi) any criminal or regulatory investigation or formal enquiry which involves the licensee, or any of its directors or employees;
- (b) ensure that they comply with all warranties applying at the date of the commencement of the professional indemnity policies and any continuing warranties applying during the duration of the professional indemnity insurance policy;
  - (c) ensure that they make all notifications and disclosures which are required to be made to their professional indemnity insurers during the duration of the policy pursuant to its terms and conditions.
- (2) A licensee must notify their professional indemnity insurers, through the broker where appropriate, within fourteen days of the following events, or such earlier period as is specified in the professional indemnity policy, -
- (a) the details of any conditions imposed on the licensee under section 7 of the Law;
  - (b) the revocation of the licensee's licence under section 9 of the Law;
  - (c) any regulatory penalty taken by the Commission, against the licensee, or any of its directors or employees under the Law, the FSC Law, or any of the Regulatory Laws;
  - (d) any prohibition order made against the licensee, or any of its directors or employees;
  - (e) any criminal proceedings commenced against the licensee, or any of its directors or employees; and

- (f) any criminal or regulatory investigation or formal enquiry which involves the licensee, or any of its directors or employees.
- (3) A licensee must notify the Commission of the following events immediately –
- (a) any actual or purported termination, avoidance, or invalidation of the licensee's professional indemnity cover; or
  - (b) any notification made by a licensee to his professional indemnity insurers with respect to a claim, or potential claim, which may be made by the licensee under its professional indemnity policy.

#### 7.6 Reporting to the Commission

- (1) All insurance managers must obtain prior written consent, from the Commission, for any changes to outsourcing arrangements.
- (2) All insurance managers must inform the Commission, within seven days, of –
  - (a) the instigation of any criminal proceedings against the licensee, any of its directors or employees;
  - (b) any involvement, in any way, of any of its directors or employees in any regulatory or criminal investigation or enquiry; and
  - (c) any material change to the business plan.
- (3) All insurance managers must notify the Commission of the following events and provide a plan for remedial action –
  - (a) any breaches of a solvency or insurance requirement and any other breach of the Minimum Criteria for Licensing under Schedule 4 of the Law; and

## Excerpt from the Insurance Intermediaries Rules

### Part 7 Conduct of Business

#### 7.8 Professional indemnity insurance

7.8.1 A licensee must maintain adequate insurance at all times, commensurate with the size and nature of its business activities. Such cover must include professional indemnity insurance and insurance against employee dishonesty or fraud as required by this section.

7.8

#### 7.8.17.8.2 Minimum requirement

(1) A licensee must maintain the minimum cover as laid out in subsection (2). The board is responsible for ensuring that the insurance arrangements for the licensee are adequate. Where the licensee concludes that amount of insurance required for the size and nature of its business is greater than the maximum amount in (2)(b) then the amount of cover the licensee is required to maintain is the higher amount.

(1)(2) Subject to subsection (3) eEvery licensee must maintain professional indemnity insurance and employee dishonesty or fraud insurance with the following minimum limits –

(a) on the basis of each and every loss cover of at least £250,000£1,000,000; and

(b) —(b) on an annual basis, £1,000,000 or three times fee-income from regulated activitiesincome, whichever is the greater., but the Commission reserves the right to vary, in writing, these amounts in relation to individual licensees, where it considers it appropriate to do so.



### Guidance

The income from regulated activities should be based on the latest audited financial statements at the time of the relevant insurance renewal.

For the avoidance of doubt, insurance cover based on a prior year's audited financial statements does not need to be amended before the next annual renewal following the release of the following year's financial statements. However, a licensee is expected to consider whether additional cover should be arranged with immediate effect in the event that the audited financial statements show a material increase in regulatory income.

- (3) Where the licensee also carries out unregulated activities, the licensee must consider whether the minimum indemnity limit of its insurance policies and scope of the insurance cover are appropriate for its businesses as a whole, taking into account possible claims that may also arise from unregulated businesses.
- (4) Notwithstanding Rule 7.8.2(2), above, a licensee is not required to have aggregate insurance cover exceeding £10,000,000 provided that the Board of the licensee has considered and decided that such level of cover is appropriate and sufficient for its business. The licensee must be able to evidence the Board's assessment if requested by the Commission.

### Guidance

The consideration by a licensee of its insurance requirements should be clearly documented at local board or senior management level to demonstrate how the decision was made. The Commission expects all licensees, whether or not they are part of organisations with offices elsewhere, to consider the insurance requirements for the entities in the Bailiwick of Guernsey.

Where a local operation is part of a group and the local board or management do not consider the cover available to the Guernsey licensee to be adequate the Commission expects the board or management to make arrangements to maintain appropriate cover. This may include purchasing a separate policy for the local operation.

~~(2)~~(5) Where the deductible or excess exceeds £20,000, on the basis of each and every loss, the minimum capital requirement will increase to 125% of the deductible or excess.

(6) A licensee must maintain at all times cover for:

- (a) negligence, errors or omissions by the licensee or its employees;
- (b) any liability for the dishonest or fraudulent acts of employees which may fall on the licensee;
- (c) liabilities of its employees who, in the course of their duties to the licensee, perform functions in their own names;
- (d) liabilities which the licensee might incur in any jurisdiction in which it should reasonably foresee that it may be held liable for damages and costs;
- (e) where relevant, ombudsman awards; and
- (f) legal defence costs.

(7) The retroactive date for the insurance arrangements in this section must be the date the licensee was licensed by the Commission.

#### 7.8.27.8.3 Notifications to the insurer

(1) A licensee must –

- (a) when applying for cover, notify his professional indemnity insurer, through his broker where appropriate, of all material facts including and without limitation –
  - (i) details of any condition imposed on the licensee, under section 7 of the Law;
  - (ii) revocation of the licensee's licence, under section 9 of the Law;
  - (iii) any regulatory penalty taken by the Commission against the licensee, or any of its directors or employees, under the FSC Law, or any of the Regulatory Laws;