Direct line: 0300 500 0597
Local fax:
Email: LifeInsurancePortfolioCommunications@fca.org.uk

FINANCIAL CONDUCT AUTHORITY
12 Endeavour Square
London
E20 1JN

Tel +44 (0)20 7066 1000
Fax +44 (0)20 7066 1099
www.fca.org.uk

6 December 2018

Dear CEO

**Risks Life Insurance firms pose to consumers or markets**

The purpose of this letter is to set out our view of the key risks of harm Life Insurance firms pose to their customers or the markets in which they operate. You should consider the degree to which your firm presents these risks and your strategies for mitigating them.

Our Life Insurance supervision strategy covers a 2-year period, which began in April 2018. This strategy includes the programme of work to identify, diagnose and remedy the harm that Life Insurers may cause, and to evaluate the impact of our interventions. We will write to you again at the end of this period to provide you with our updated view of the sector key risks and our updated supervisory plans.

**Our view of the key drivers of harm**

We see three key ways in which customers may be harmed:

- Customers have reduced levels of savings and lower levels of income in retirement due to poor management of their funds.
- Customers are not provided with the investment, pension or protection product or service they expected because of changes to or unclear terms and conditions.
- Customers do not receive the service or payments they expect because of operational failures.

To assess how these types of harm arise, we have analysed the strategies, business models, and the drivers of culture (including the governance arrangements and purpose) of firms in the Life Insurance sector.

The long-term nature of many of the products manufactured and sold by Life Insurers means outcomes can emerge over very long periods of time, making it difficult at times to assess the consequences of customers' decisions. It also means that customers can have very little or no time to take corrective action if they experience unexpected or poor outcomes.

The complexity of some products, infrequent engagement between their providers and customers, low levels of understanding of financial products among some customers, and inherent conflicts of interest between different customer groups as well as between customers and different stakeholder groups, are all factors Life Insurers should consider when pursuing their strategies and in their oversight and controls arrangements.

Long-term and complex insurance-based products come with the inherent risk of mis-alignment of purpose and incentives between firms, their staff and their customers. A firm's leadership and governance play a key role in driving a culture in which there is appropriate focus on meeting our published expectations relating to the consumer outcomes that firms should strive to achieve[1].

**Our areas of focus**

We will prioritise our supervisory work in the following areas:

**Culture and Governance**: flaws in firms' culture and governance are often the root cause of harm to consumers. Whilst good governance is important in every sector, it plays an especially critical role in this sector, given its long-term and complex product features described above. Your firm must be governed effectively and it is important that individuals are held accountable for their actions.

We will engage with individual firms to assess their culture and governance arrangements, and in doing so will test the extent to which they and their Senior Managers are able to demonstrate to us the effectiveness of their governance arrangements in identifying, managing and mitigating the risk of harm. Our assessment will be based on an established framework, through which we will discuss with all Life Insurers how they manage conduct risk against a clear framework. This approach will allow us to compare how they do so, and to what extent their programmes for improving conduct enable them to challenge themselves and benchmark their efforts across the sector. We expect this work to commence in Q2 2019.

**Resilience and Outsourcing**: the information held by Life Insurers, and the significant reliance many of their customers place on reliability of service, means that when things go wrong with their outsourced services arrangements there is a potential to affect millions of consumers. In July the FCA, PRA and BoE published a joint discussion paper on resilience and we will be working with the PRA to assess the business continuity and recovery plans firms have in place in the event of such failures.

Through information provided to us by firms and subsequent on-site assessments, we will test the extent to which they have clear and effective oversight of their outsourcing activities, as well as their disaster recovery and continuity of service arrangements. This work is underway and will progress through the first half of 2019.

**Unit-linked funds**: customers across c.29m policies are invested in unit-linked funds in the UK, and there have been several examples of poor governance and controls which have caused harm to these customers. Our Asset Management Market Study highlighted evidence of weak governance over authorised funds in terms of the value they provide to consumers, and this has prompted us to pursue governance remedies with these funds.

We have committed to evaluating whether similar governance remedies may be appropriate in unit-linked funds. In doing so, we have been examining how a number of firms assess whether they are delivering value for money to unit-linked customers. This analysis is already

---

[1] https://www.fca.org.uk/firms/fair-treatment-customers

underway and entails our assessment of the current practices and governance arrangements across a number of firms.

We are also commencing analysis of how firms which operate 'mirror' funds provide the outcomes consumers expect. We expect to complete this towards the end of Q1 2019.

**With-profit funds**: customers holding c.14m with-profits policies rely on the effective management of with-profits funds and they remain a core part of the business models of many Life Insurers. The inherent conflicts of interest and the declining books of with-profits business increase the risk of harm occurring through, for example, the unfair treatment of policyholders.

We commenced a review in June 2017 which seeks to understand how firms across the sector manage customer interests in many priority areas. Through information provided to us by these firms, and subsequent discussions with their Senior Managers, we will test the extent to which, in the decisions and actions they and their firms take, Senior Managers fully understand the impact these may have on their with-profits customers. We expect to conclude this work in the first half of 2019.

**Long-standing customers**: the long-term nature of the products and services delivered by Life Insurers means the fair treatment of long-standing customers is central to delivering good customer outcomes. We will evaluate the impact of the Finalised Guidance 16/8 we published following our review in this area. We will also be inviting firms to participate in an industry roundtable to discuss the progress made.

The aim of the Finalised Guidance is to change firm behaviour, rather than to correct specific features of the market that may drive poor outcomes. Our evaluation will test the extent of this behavioural change and if the decisions and actions Senior Managers take result in driving better outcomes for closed-book customers. The industry roundtable will inform our approach in how we take forward the full evaluation. We plan to commence this work in the second quarter of 2019.

**Senior Managers and Certification Regime (SM&CR)**: we will undertake work to assess how firms are implementing the SM&CR. As is reflected throughout our priority areas of focus, we will also test the extent to which Life Insurers who will become subject to the SM&CR are able to demonstrate to us they have implemented the Regime effectively. This work will involve us reviewing how firms have identified, assigned and documented Senior Managers' responsibilities (including through their Statements of Responsibility), to coincide with the extended regime coming into force. This work is planned for the first half of 2019.

**EU withdrawal**: in conjunction with the PRA, we will continue to assess firms' plans for the UK's withdrawal from the EU and the impact these plans may have on consumers. As your firm prepares for EU withdrawal, it is important that your Senior Managers ensure execution is managed appropriately. In the context of the political and regulatory preparations being made for March 2019, we expect firms to concentrate on planning for 'Day One' readiness for their EU27 customers. For these reasons, firms should focus on ensuring that they make the minimum necessary changes required to avoid harm to the clients they serve or markets in which they operate, and that these changes are in their customers' best interests.

**LIBOR transition:** As we have previously highlighted[2], there is support to sustain LIBOR until the end of 2021, but firms should treat its discontinuation after that date as something that will happen and which they must be prepared for. It is important that firms' Senior Managers and Boards are taking appropriate action now so that their firms can transition to alternative rates ahead of end-2021. In our ongoing engagement with them, we will assess the extent to which they understand the risks associated with this transition, and the steps they are taking to mitigate those risks.

**Next steps**

If you have any questions please contact your normal supervisory contact on 0300 500 0597. This is the primary point of contact for your firm's day-to-day interactions with the FCA, and further details of how we can be reached are available on our website at:

https://www.fca.org.uk/contact

However, we recognise that there may be occasions in which your firm faces urgent issues of strategic importance. In such significant circumstances, please contact Caroline Gardner on 020 7066 8186.

Yours sincerely

Debbie Gupta

Debbie Gupta
Director
Life Insurance and Financial Advice

---

[2] https://www.fca.org.uk/publication/correspondence/dear-ceo-letter-firms-transition-from-libor-insurers.pdf