Professional Indemnity Insurance – Investment Firms

Following the announcement from the FCA to increase the Financial Ombudsman Service award limit to £350,000, The SimplyBiz Group published notice of this on 14th March 2019. This was subsequently followed up by a further bulletin, on 1st April 2019, at the time we became aware the FCA was contacting firms to ensure their professional indemnity insurance (PII) covered them for this increase.

This was particularly relevant for those firms that held full pension transfer permissions. Many PII providers took this as an opportunity to review their liabilities within this area of the market. The outcome of those reviews has led to some firms now holding cover that does not meet FCA’s Prudential rules (IPRU-INV 13) for PII requirements.

What action you need to carry out now and at renewal

You need to check the terms on your PII policy to ensure it does not:

- Exclude DB pension transfer activity
- Limit the coverage against the full FOS award limit
- Limit the number of cases you are able to advise on (this includes advice to remain in the scheme as well as transfer)
- Limit the aggregate case amount
- Include an excess above £5,000 for DB transfers and other investment business

Do any of the above apply to your firm? If so and you have advised on defined benefits schemes or intend to do so in future, please consider your position(s) as set out below. Some of these issues may also be relevant to those firms that do not hold the full pension transfer permission:

Excluded DB pension transfer activity

If this activity is now excluded from your policy, it is our recommendation you do NOT advise on any future DB schemes*. You will however need to consider the past DB transfer activity carried out, as the firm will be subject to any liabilities arising from this. It is always difficult to foresee any specific business written resulting in a future claim, let alone the amount of resulting redress. For this reason, the FCA has set out in a table the additional capital a firm must hold to meet the capital requirements. This is linked solely to the firm’s relevant income as listed under IPRU-INV 13.1.23 here, however, it then states firms should hold additional capital on top of this, where that amount would provide insufficient cover accounting for the circumstances of the firm. To determine whether you hold sufficient cover or not, it would be dependent on, but not limited to:

- The number (volume) of advised clients
- Number of transfers completed
- The number of insistent clients
- The average case size
- The ceding scheme
- The accepting scheme and investment solution
- Outcome of independent file reviews
- Past complaints

Before determining if you need to hold any further capital, or the amount of this, you should speak with our Compliance Helpdesk to discuss your personal situation in more detail.
*It is The SimplyBiz Group’s view that no activity should be carried out that requires full self-insurance. Given the higher-risk nature of advising on transfers, only after obtaining FCA consent should you give any consideration to self-insuring.

**Limited coverage against the full FOS award limit**

In the event of an upheld complaint awarded by the FOS, the firm would be liable for the difference between the PII award limit on your policy and that determined by the FOS, being potentially up to £200,000 (new limit of £350,000 less previous limit of £150,000). As the PII policy would not meet the FCA’s required rules for holding PII, the firm would need to consider self-insuring through its financial resources.

In the first instance, you would need to determine the number of advised clients where the potential liability could exceed the stated FOS award limit on your policy. Once identified you should then consider the following, although not exhaustive:

- The number of insistent clients
- The ceding scheme
- The accepting scheme and investment solution
- Outcome of independent file reviews
- Past complaints

The SimplyBiz Group holds the view that in the event where a firm determines they do not have exposure to liabilities above the stated FOS award limit, additional capital should still be maintained where any client has, or had, a DB scheme transfer value which exceeded the FOS award limit as stated within your PII policy terms. For this purpose, we would recommend using table IPRU-INV 13.1.23 here after speaking in the first instance with our Compliance Helpdesk.

**Limiting the number of cases**

You should ensure you do not exceed the number of cases limited by your PII policy. Once the number of transfer cases is reached, you should notify your insurer immediately. Should this number be exceeded without notification, it would likely invalidate the terms of the policy and result in the firm having to self-insure for all DB transfer activity carried out in the past. A further likely consequence is that this would also result in DB transfers then being fully excluded thereafter.

**Limited aggregated amount**

This is where, for example, the aggregate liability on the policy would be limited to £500,000. Any redress during the term that exceeded the collective amount (£500,000) from paid claims would not be met by the insurer and therefore the firm would have to self-insure those amounts.

In these circumstances, firms should monitor and aggregate all claims paid out during the policy term and determine the extent of their potential liabilities as highlighted in earlier sections, as to whether there would be a need to hold further capital.

**Increased excess (above £5,000 for DB transfers and any other type of investment business)**

Where your PII excess (under any policy line) exceeds £5,000, the FCA sets out its Prudential rules prescribed additional amounts a firm must hold in its capital requirements. This is based on the amount of the excess, and the firm’s relevant income, and is set out under IPRU-INV 13.1.27 here

This amount is in addition to your existing capital adequacy requirement (minimum £20,000).
This amount would not include consideration to any limitations to the maximum FOS award amount as described above.

**Removal of the full Pension Transfer Permission or ceasing to provide further advice**

If your permission for this activity has been removed, or you are no longer going to provide future advice, through choice or otherwise, you will still need to insure past business and therefore the above situations will still be relevant to you.

**Applying for Pension Transfer Activity**

For those firms considering applying for this activity it is likely that as you do not hold any past exposure in this line of business, you will obtain favourable PII terms. **PLEASE NOTE** however that when this becomes due for renewal at future anniversaries of the policy, it is possible that some of the above situations will arise within the policy terms and therefore you should give future consideration to these important areas.

**Firms NOT holding the full Pension Transfer permission but subject to any of the above restrictions or exclusions**

The same principles apply to all other types of business where additional capital requirements are prescribed by the FCA by referring to the appropriate table in IPRU-INV. You need to review your policy and any endorsements carefully.

Should you determine further capital is required to meet any potential claims, you may wish to speak with our Compliance Helpdesk to discuss your personal situation.

**Holding additional capital**

Where you are required to hold additional capital due to any of the above situations, you must hold this in line with your existing ‘own funds’ requirements and this additional amount must be ‘readily realisable’, the definition of which means this amount must be readily available within 90 days.

**Notification to the FCA**

You must immediately notify FCA in instances where any of the following applies:

- The aggregated amount of cover is exhausted
- You are not covered for business lines which have been carried out
- Cover is being self-insured by an amount not prescribed by a relevant FCA table

Where the firm has personally determined the amount of additional capital it requires to self-insure, the firm when notifying the FCA should confirm the basis of their calculation.

**ALL FIRMS**

It is important to review the terms of your PII policy at renewal and throughout its term, to ensure you are aware of its coverage, any limitations placed upon the activities of the firm and whether any breaches have occurred during the period of cover.

If you have any further queries or if your situation is not covered by any of the above scenarios, please do not hesitate to contact our Compliance Helpdesk.