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INSURANCE REGULATORY EBULLETIN

ROUND UP OF REGULATORY DEVELOPMENTS IN JUNE
2020



WELCOME TO OUR INSURANCE REGULATORY EBULLETIN

Welcome to this edition of our Insurance Regulatory eBulletin, which aims to keep you updated with significant regulatory developments and their implications across the insurance sector.

I hope you and your families continue to be safe and well. Whilst there seems to be some light at the end of the tunnel with the start of the easing of some of the lockdown restrictions I suspect it will be some time still before some sort of normality returns. While, this unusual situation continues, we continue to operate and serve our clients as a fully-remote, fully-connected workforce.

June has again been a busy month on the regulatory front as a result of the implications of COVID-19 for both prudential and conduct regulation. The regulators in Europe and the UK continue to defer making and proposing new policy but continue to emphasise their focus on ensuring the insurance sector is both financially resilient and treating its customers fairly. The PRA have provided feedback on its Insurance Stress Test 2019 and related COVID-19 stress testing and the Treasury has announced a review of Solvency II in preparation for a post-Brexit world. The FCA is pressing on with its test case on business interruption insurance and will have a new Chief Executive in the autumn. Jointly the PRA and FCA have released the Climate Financial Risk Forum's initial guidance on climate change to assist firms in approaching and addressing climate-related financial risk management.

This bulletin contains as much up to date regulatory news as we can gather. Inevitably, this may change as the current situation develops and we will aim to keep you informed in the future.

Please do not hesitate to contact myself or your normal BDO contact if you have any concerns over any matter highlighted in this update.

Say safe and stay well and I hope you enjoy reading this latest update.



ALEX BARNES
PARTNER

+44 (0)20 7651 1213
alex.barnes@bdo.co.uk

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EIOPA

EIOPA MONITORING OF LIQUIDITY RISKS IN THE INSURANCE SECTOR

On 9 June, EIOPA issued a [statement](#) supporting the European Systemic Risk Board (ESRB) on the importance of improving the monitoring of liquidity risks in the insurance sector to enhance Europe's preparedness for potential future economic shocks.

As a response to COVID-19, EIOPA has already developed and put in place a proportionate framework to enhance the nature and the consistency of the information collected on liquidity risks. EIOPA notes that there is no current evidence of the materialisation of liquidity risks in the insurance sector.

As part of the Solvency II Review, EIOPA has consulted on proposals to reinforce the macro-prudential elements of the regime, including strengthening the tools available to assess and monitor liquidity risks. The proposals will be re-assessed in light of any COVID-19 evidence.

EIOPA RESPONDS TO CONSULTATION ON THE REVISION OF THE NON-FINANCIAL REPORTING DIRECTIVE

On 11 June, EIOPA [responded](#) to the EC's consultation on revising the Non-Financial Reporting Directive (NFRD).

EIOPA welcomed the initiative to revise the NFRD in the light of insurance undertakings and pension funds being important to investing in long-term, sustainable investments and the related integration of environmental, social and governance (ESG) factors. It believes sustainable investment opportunities and an effective integration of ESG factors, requires high quality non-financial reporting.

The European Banking Authority (EBA) and the European Securities and Markets Authority (ESMA) also provided responses to the consultation. Along with these individual responses, EBA, EIOPA and ESMA submitted a [joint letter](#) from their Chairs, highlighting the

key messages for Europe's future non-financial reporting regime.

EIOPA REPORTS ON ITS ACTIVITY AND SUPERVISION IN 2019

On 15 June, EIOPA published its [Consolidated Annual Activity Report](#) (CAAR) for 2019. The report covers how EIOPA has met its strategic objectives for 2019 which were:

- ▶ Driving forward conduct of business regulation and supervision;
- ▶ Leading convergence towards high-quality prudential supervision throughout the EU;
- ▶ Strengthening the financial stability of the insurance and occupational pension sectors;
- ▶ Delivering EIOPA's mandate effectively and efficiently;
- ▶ Working on the following cross-sector priorities;
- ▶ Sustainable finance, including climate change; and
- ▶ InsurTech, including Big Data and cyber risk.

On 17 June, EIOPA [reported](#) on its supervisory activities in 2019. EIOPA's overall objective in this area is to promote a high, effective and consistent level of supervision throughout the EU.

The work focused on the priorities identified in the Supervisory Convergence work plan for 2019 as well on prudential and conduct issues that emerged during the year. The priorities were:

- ▶ Implementing a common supervisory culture and further development of supervisory tools;
- ▶ Identifying risks to the internal market and its level playing field;
- ▶ Supervision of emerging risks; and
- ▶ Oversight activities.

The report sets out examples of EIOPA activities for each of the work plan priorities.

The report also sets EIOPA's 2020 priorities which are:

- ▶ Supporting the supervisory capacity of NCAs and supervisory convergence;
- ▶ Focusing on cross-border and third country activities; and
- ▶ Further investigating possible conduct risks.

RESULTS OF THE REGULAR SUPERVISORY REPORT PEER REVIEW

On 18 June, EIOPA published the findings of its [peer review](#) of the Regular Supervisory Report (RSR). The peer review set out to examine to what extent the proportionate approach set out under the Delegated Regulation has been implemented among the EU's national competent authorities (NCAs) and also to determine whether further convergence is needed on the frequency of submission of RSRs.

EIOPA issued 51 recommended actions to 26 NCAs as a result of the review. The recommended actions target supervisory shortcomings which NCAs are expected to have implemented by 2022.

The findings of the peer review, also led EIOPA to conclude that the SII legislation needs further clarification. The following improvements are needed to achieve supervisory convergence:

- ▶ Introducing supervisory guidance on keeping the minimum requirement for submission of the full RSR as once every 3 years; and
- ▶ Further guidance for NCAs on how to ensure proportionality in deciding on the frequency of full RSR submission based on a list of events that are specific to the undertaking (such as mergers and acquisitions).

DISCUSSION PAPER ON METHODOLOGICAL PRINCIPLES FOR INSURANCE STRESS TESTING

On 24 June, EIOPA issued a [second Discussion Paper](#) (DP) on the methodological principles for insurance stress testing. The DP is part of a broader process to enhance EIOPA's stress testing framework and sets out EIOPA's work on the following topics:

- ▶ A stress test framework on climate change;

- ▶ An approach to liquidity stress testing; and
- ▶ A multi-period framework for bottom-up insurance stress testing.

Comments on the DP are to be submitted by 2 October 2020 using the template provided.

EIOPA'S RESPONSE TO THE EC'S DIGITAL FINANCE STRATEGY CONSULTATION

On 29 June, EIOPA [responded](#) to the EC's consultation on a new digital finance strategy for Europe. EIOPA highlighted that a sound approach to financial innovation should strike a balance between enhancing financial innovation and ensuring well-functioning consumer protection and financial stability frameworks. EIOPA believes a level playing field and technological neutrality are crucial.

EIOPA considers that further improvements can be achieved in the following areas:

- ▶ Insurance regulation being fit for purpose by understanding how new technologies and business models drive new risks and opportunities.
- ▶ A fair, ethical and transparent use of data. Data analytics governance frameworks are crucial in engendering trust and grounding the use of data in common ethical principles.
- ▶ Access to relevant datasets such as:
 - Open Finance/Open Insurance
 - Internet of things data
 - Cyber incident reporting data
 - Data standardisation

PRUDENTIAL REGULATION

PRA STATEMENT ON THE USE OF ELECTRONIC SIGNATURES

On 2 June, the PRA issued a [statement](#) on the acceptability of electronic rather than ‘wet’ signatures (i.e. signing a document by hand using a pen) in relation to the submission of forms and other regulatory documents in the context of COVID-19 and increased remote working.

The PRA confirmed that, in the absence of any specific legal provisions to the contrary, firms may use electronic signatures for such purposes, although it may in specific instances request a ‘wet signature’.

The PRA specifically noted it was unable to comment on the use of electronic signatures more generally, and firms should obtain their own legal advice on the validity of such signatures and also reminded firms on the Rulebook requirements for adequate systems and controls.

JOINT STATEMENT BY THE BANK AND PRA ON THE ESRB RECOMMENDATIONS FOR THE RESTRICTION OF DISTRIBUTIONS

On 8 June, the PRA and Bank of England (the Bank) issued a [joint statement](#) regarding a Recommendation by the European Systemic Risk Board (ESRB) in relation to the restriction of distributions during the COVID-19 pandemic. The Recommendation applies to the UK during the transition period before Brexit.

The Bank and PRA have previously announced various measures to ensure the resilience of the financial system, to support banks’ lending and to maintain the safety and soundness of firms.

Since the existing measures are consistent with the ESRB’s Recommendation, the PRA and Bank do not consider it necessary to extend their guidance further at this time.

INSURANCE STRESS TEST 2019 FEEDBACK

On 17 June, the PRA provided [feedback](#) to participating firms on the results of the 2019

Insurance Stress Test (IST 2019) exercise and its more recent activity on COVID-19 stresses.

IST 2019 was the third PRA exercise for general insurers and the first for life insurers since the introduction of Solvency II. It incorporated asset and liability shock scenarios as well as a number of exploratory scenarios, including a climate change exercise. For general insurers it also included a joint exercise with the Bermuda Monetary Authority (BMA) for natural catastrophe scenarios, in support of the joint commitment to supervisory cooperation.

The COVID-19 element of IST 2019 concluded that overall the insurance sector is robust to downside stresses, with the highest uncertainty focused on the liabilities of certain general insurers.

For general insurers, IST 2019 suggested that the industry is resilient to natural catastrophe risks, in common with the Bermuda-based reinsurers.

The PRA noted three areas for further work by industry on estimating insured losses from natural catastrophe scenarios:

- ▶ Allowing for risks not captured within standard models (such as contingent business interruption, or types of event, such as a secondary peril).
- ▶ Allowing for secondary perils in light of recent experience (such as inland flooding following a hurricane).
- ▶ Data quality.

The exploratory scenarios identified further development in the industry’s ability to assess cyber-related and sectoral (across economic sector) exposures is required.

The PRA will work with insurers on taking the findings of IST 2019 forward. They expect boards to assess whether the findings apply to their firm and present an action plan to their supervisors to address these.

PRA ANNUAL REPORT 2019/20

On 18 June, the PRA published its [Annual Report](#) for the year ended 29 February 2020.

The report describes how the PRA has discharged its functions and how its goals have been advanced taking into account both its regulatory principles and the requirement to facilitate effective competition in the markets.

GOVERNMENT ANNOUNCES SOLVENCY II REVIEW

On 23 June, HM Treasury announced plans for a review of the Solvency II regime to take place in the autumn. The review is part of a package of measures for financial services after Brexit, unveiled by the Chancellor in a [Written Ministerial Statement](#).

The review aims to ensure the Solvency II regime is “properly tailored to take account of the structural features of the UK insurance sector”. It will consider areas that have been the subject of long-standing discussion while the UK was an EU Member State, some of which may also form part of the EU’s own Solvency II review. The review will include, but is not limited to, the risk margin, the matching adjustment, the operation of internal models and reporting requirements for insurers.

The Government expects to publish a Call for Evidence in the autumn.

COVID-19 REGULATORY REPORTING AMENDMENTS - UPDATE

On 23 March, the PRA announced that as part of its response to COVID-19, the Regulatory Supervisory Report (RSR) was not required for year-end 2019. (This applies to firms with a 31 December 2019 year-end, or year-ends after that date but before 1 April 2020).

On 24 June, the PRA [provided clarification](#) on RSR submissions for year-end 2020 onwards.

The PRA considers that the existing RSR cycle (i.e. a full report at least every three years and in summary every year) should continue. Therefore, firms with year-ends on 31 December 2019 or before 1 April 2020 due to submit a full report for year-end 2019 will be required to submit summary reports for year-end 2020 and

year-end 2021, and a full report for year-end 2022.

In line with its update on 16 April 2020, the PRA considers COVID-19 to be a major development, and therefore expects year-end 2020 RSR reports to include information on the impact of COVID-19.

THE CLIMATE FINANCIAL RISK FORUM PUBLISHES GUIDANCE

On 29 June, the Climate Financial Risk Forum (CFRF), jointly established by the PRA and the FCA, published a guide designed to assist businesses in approaching and addressing climate-related financial risk management.

The guide sets out practical recommendations to firms of all sizes on the disclosure of climate-related financial risks, efficient risk management, scenario analysis, and opportunities for innovation in the interest of consumers. The guide aims to help the financial services sector cope with the significant challenges and risks associated with climate change.

The guide contains four industry-produced chapters ([Risk Management](#), [Scenario Analysis](#), [Disclosures](#), and [Innovation](#)) and a [Summary](#) co-produced by the FCA and PRA.

Whilst the PRA and FCA have convened and facilitated the CFRF discussions, the views expressed in the guide do not necessarily represent the view of the regulators and therefore does not constitute regulatory guidance.

SOLVENCY II TECHNICAL INFORMATION CONSULTATION - CP 5/20

On 30 June, the PRA published a [Consultation Paper \(CP 5/20\)](#) setting out its proposed approach to the publication of Solvency II technical information (TI) after the end of the transition period (TP). The proposals included in the CP, which would apply at the end of the TP, are:

- ▶ the PRA’s published TI would be derived by adopting the same technical methodologies embodied within EIOPA’s TI as at the end of the TP, with some limited exceptions. The

exceptions are set out in a [draft Statement of Policy \(SoP\)](#), and are generally items requiring change as a result of Brexit, and the resulting changes to information flows between the PRA and EIOPA. The changes also contribute to the TI being relevant and credible for UK firms.

- ▶ the criteria that the PRA would use to determine the PRA relevant currencies to publish, which would be based on the relative materiality of technical provisions denominated in each currency, and the currencies for which firms have volatility adjustment (VA) or matching adjustment (MA) authorisation.
- ▶ the PRA's approach to determining VA reference portfolios (which would inform the calculation of the VA), in light of the loss of sharing of regulatory returns data between the PRA and EIOPA; and
- ▶ the publication of TI on the PRA website, and, where there is a deviation in the future from EIOPA's technical methodology, a PRA publication that describes this deviation.

The CP is relevant to all UK Solvency II firms, including in respect of the Solvency II groups provisions, to the Society of Lloyd's and its managing agents. Non-Directive firms are outside the scope of the CP.

The PRA invites feedback on the proposals by 30 September 2020.

CONDUCT REGULATION

MUTUAL SOCIETIES REGISTRATION FUNCTION: 2019-20

On 29 May, the FCA has [issued an overview](#) of developments on the mutual societies registration function in 2019-20. The update provides an overview of the function, details of developments in the past year, and some statistical information on the work of the FCA and the number of societies on the register.

The update covers, amongst other things, the Mutuals Public Register; the Mutuals Society Portal; fees; application forms; and reviews of processes in response to the COVID-19 pandemic.

BUSINESS INTERRUPTION INSURANCE TEST CASE: DRAFT GUIDANCE

On 1 June, the FCA outlined [its expectations](#) for insurers and insurance intermediaries when handling claims and complaints for business interruption policies during its test case.

The guidance highlights specific steps that firms should be taking to identify any potential implications of the test case on decisions to reject claims; keep policyholders informed about the test case and the implications for policies, claims and any settlement offers; and treat policyholders fairly when the test case is resolved.

Insurers who are accepting claims or have determined their policies respond are expected to continue handling claims in accordance with their current approach and to pay agreed claims on a timely basis.

PRODUCT VALUE AND CORONAVIRUS: GUIDANCE FOR INSURANCE FIRMS

On 3 June, the FCA confirmed [guidance](#) setting out its expectations for insurers and insurance intermediaries to consider the value of their products in light of the exceptional circumstances arising from COVID-19. It also published a [Feedback Statement \(FS20/7\)](#) on the guidance consultation.

The guidance sets out what the FCA considers firms should be doing to identify any material

issues that affect the value of the general insurance and protection products they offer, and their ability to deliver good customer outcomes, during this unprecedented time.

It sets out that firms should focus on reviewing products where benefits cannot be provided (e.g. boiler services due to lockdown measures) or where there has been a fundamental change in risk and products are now providing little or no utility to customers (e.g. public liability insurance for closed businesses).

The guidance is not intended to create an expectation that firms should reassess the value of insurance products where the likelihood of a customer making certain claims may have fallen, but the product continues to provide utility (e.g. motor insurance where, for example, theft or fire can still occur).

Firms should review their product lines and decide on any resulting actions within 6 months. This might include changing how benefits are delivered, refunding some premiums or suspending monthly payments for a certain period of time.

The guidance came into immediate effect and will be reviewed in 6 months in light of developments regarding coronavirus and may be revised if appropriate.

The guidance is relevant to all insurance products, whether the customer is retail or commercial, including natural persons (i.e. individuals) and business customers, and comes into force with immediate effect.

FCA BOARD MINUTES: 30 APRIL 2020

On 4 June, the FCA published the [minutes](#) of the FCA Board meeting held on 30 April 2020. After a report from the Chief Executive on business interruption insurance and the Coronavirus Business Interruption Loan Scheme (CBILS), the Board discussed a number of topics including:

- ▶ the macro-economic implications of the Covid-19 pandemic;
- ▶ the FCA's response to Covid-19;

- ▶ COVID-19 Insurance and Premium Finance Guidance;
- ▶ a report from the PRA; and
- ▶ A briefing on compensatory payments under the Complaints Scheme.

BUSINESS INTERRUPTION INSURANCE

Throughout June, the FCA has released updates to the [information](#) on how it is seeking legal clarity on business interruption (BI) insurance during the coronavirus (COVID-19) crisis.

The FCA intends to obtain court declarations as part of a test case, aimed at resolving the contractual uncertainty around the validity of many BI claims.

The result of the test case will be legally binding on the insurers that are parties to the test case in respect of the interpretation of the representative sample of policy wordings considered by the court. It will also provide persuasive guidance for the interpretation of similar policy wordings and claims, which can be taken into account in other court cases including in Scotland and Northern Ireland, by the Financial Ombudsman Service and by the FCA in looking at whether insurers are handling claims fairly.

NIKHIL RATHI APPOINTED AS NEW CHIEF EXECUTIVE OF THE FCA

On 22 June, HM Treasury [announced](#) the appointment of Nikhil Rathi as the new permanent Chief Executive of the FCA.

He is currently the Chief Executive of London Stock Exchange plc. From September 2009 to April 2014, he was Director, Financial Services Group at HM Treasury. In this role, he led the Treasury's work on the UK's EU and international financial services interests. He is expected to take up his new role in the Autumn.

FCA SERVICE STANDARDS 2019/20

On 24 June, the FCA published [an overview](#) of its performance in 2019/20 in a number of areas, covering both statutory standards and voluntary commitments. It sets out 60 service standards on activities related to regulatory applications, telephone enquiries and other correspondence.

FCA BOARD MINUTES: 13 MAY 2020

On 25 June, the FCA released the [minutes](#) of its 13 May 2020 Board meeting. The minutes include:

- ▶ an update from the Chief Executive on the FCA's activities and priorities in response to the COVID-19 pandemic;
- ▶ the Board Approval on the publication of guidance clarifying the expectations of insurance and premium finance firms dealing with consumers in temporary financial difficulties, as a result of COVID-19; and
- ▶ a briefing on the SM&CR requirements for solo-regulated firms relating to submission of assessed staff for inclusion on the Register.

CHANGES TO REGULATORY REPORTING DURING CORONAVIRUS

On 26 June, the FCA [updated its temporary measures](#) for firms submitting regulatory returns.

Firms may now apply 2-month extensions to the deadlines for certain returns due up to and including 30 September 2020, including the credit union complaints return, the complaints return and the claims management companies' complaints return.

GEFION INSURANCE A/S WITHDRAWAL OF LICENCE TO OPERATE

On 30 June, the FCA issued a statement on Gefion Insurance A/S (Gefion), an insurance firm authorised and regulated by the Danish Financial Supervisory Authority (DFSA).

The DFSA has announced that it has withdrawn Gefion's licence to operate. This means that Gefion will be unable to underwrite any new policies. Gefion operates in the UK on a freedom of services basis which means that some customers, both private and commercial, based in the UK may have a policy with the firm.

The [DFSA's press release](#) has more information, including questions and answers for policy holders.

EXTENSION OF THE SMCR IMPLEMENTATION PERIODS FOR SOLO-REGULATED FIRMS

On 30 June, the FCA [announced](#) that HM Treasury has agreed to delay the deadline for solo-regulated firms to undertake their first assessment of the fitness and propriety of their Certified Persons has been delayed from 9 December 2020 until 31 March 2021.

To ensure SMCR deadlines remain consistent, and to provide extra time for firms that need it, the FCA intend to consult on extending the deadline for the following requirements from 9 December 2020 to 31 March 2021:

- ▶ the date the Conduct Rules come into force;
- ▶ the deadline for submission of information about Directory Persons to the Register; and
- ▶ references in FCA rules to the deadline for assessing Certified Persons as fit and proper (which has been agreed by the Treasury).

The FCA emphasise:

- ▶ Senior Managers must ensure that Conduct Rules training is effective, so that staff are aware of the Conduct Rules and understand how they apply to them in their jobs. These programmes will require planning, time and effort to deliver effectively.
- ▶ Firms should continue with their programmes of work in these areas and, if they are able to certify staff earlier than March 2021, they should do so. Firms should not wait to remove staff who are not fit and proper from certified roles.

APPROVED PERSONS REGIME (APR) AND CORONAVIRUS: FCA EXPECTATIONS

On 30 June, the FCA set out its [expectations](#) for how firms using Appointed Representative (AR) arrangements apply the Approved Persons Regime (APR) during coronavirus (COVID-19).

The FCA recognise that firms may need longer periods of temporary arrangements if, for example, an Approved Person is absent because of coronavirus, or if recruitment to replace an Approved Person has been delayed due to the pandemic.

The temporary arrangements relate to:

- ▶ Temporary arrangements for controlled functions - 12-week rule extended to 36 weeks.
- ▶ Furloughed staff - can retain their approval during their absence and will not need to be re-approved by the FCA.
- ▶ Notification and documentation - the FCA do not expect firms to notify it under Form D of the temporary arrangements but do expect the temporary arrangements (however temporary) to be clearly documented internally.

Regulated firms that use ARs to carry on regulated activity remain responsible for their ARs and networks.

ENFORCEMENT ACTION

FCA REGULATORY FINES ROUND-UP

FCA regulatory fines in 2020 total [£104.7m](#). The following new fines have been announced by the PRA or FCA in the past month.

Commerzbank AG	<p>A fine of £37.8m for failing to put adequate anti-money laundering (AML) systems and controls in place between October 2012 and September 2017. Commerzbank London was aware of the weaknesses but failed to take reasonable and effective steps to fix them despite the FCA raising specific concerns about them in 2012, 2015 and 2017.</p> <p>The weaknesses also persisted during a period when the FCA was publishing guidance on steps firms could take to reduce financial crime risk as well as taking enforcement action against a number of firms in relation to AML controls. Despite these clear warnings, the failures continued.</p> <p>The FCA's investigation identified failings in a number of areas, including Commerzbank London's failure to:</p> <ul style="list-style-type: none"> ▶ Conduct timely periodic due diligence on its clients, which resulted in a significant number of existing clients not being subject to timely know-your-client checks. By 1 March 2017, 1,772 clients were overdue updated due diligence checks; ▶ Address long-standing weaknesses in its automated tool for monitoring money laundering risk on transactions for clients. For example, in 2015 Commerzbank London identified that 40 high-risk countries were missing, and 1,110 high-risk clients had not been added, to the transaction monitoring tool; and ▶ To have adequate policies and procedures in place when undertaking customer due diligence on clients.
Lloyds Bank Plc, Bank of Scotland Plc and The Mortgage Business Plc	<p>A fine of £64.1m for failures in relation to their handling of mortgage customers in payment difficulties or arrears. The banks have estimated that they will have paid approximately £300 million in redress.</p> <p>Between April 2011 and December 2015 the banks' systems and procedures for gathering information from mortgage customers in payment difficulties or arrears resulted in the banks' call handlers not consistently obtaining adequate information to assess customers' circumstances and affordability, creating a risk that customers were treated unfairly.</p> <p>The banks also employed a system that set a minimum percentage of a customer's contractual monthly payment which a call handler was authorised to accept as a payment arrangement without obtaining further authority from a more senior colleague. However, in practice, the system created a risk of inflexibility in approach, with the result that call handlers may have failed to negotiate appropriate payment arrangements for customers.</p> <p>These risks were exacerbated when, as part of a simplification programme, the banks lost a large number of personnel with mortgage collections and recoveries expertise, after which point nearly all of their mortgage arrears call handlers were new-to-role.</p>

Some of the failings were identified by the banks as early as 2011 but the steps the banks took failed fully to rectify the issues.

In July 2017, the banks implemented a group-wide customer redress scheme which included refunding all broken payment arrangement fees, arrears management fees and interest accrued on the fees and the refund of litigation fees if applied unfairly or, in some circumstances, automatically. The banks have estimated that approximately 526,000 customers will have received redress payments totalling £300 million.

CONTACTS

EXTERNAL AUDIT

ALEX BARNES

Partner & Head of Insurance
alex.barnes@bdo.co.uk

DAVID ROBERTS

Partner
david.roberts@bdo.co.uk

JOHN PERRY

Partner
john.perry@bdo.co.uk

TOM REED

Partner
tom.reed@bdo.co.uk

INTERNAL AUDIT

CHRIS BELLAIRS

Partner
christian.bellaairs@bdo.co.uk

LUKE PATTERSON

Director
luke.patterson@bdo.co.uk

REGULATORY ADVISORY

OMAR RIPON

Partner
omar.ripon@bdo.co.uk

RICHARD BARNWELL

Partner
richard.barnwell@bdo.co.uk

CHARLES PORTSMOUTH

Director
charles.portsmouth@bdo.co.uk

ACCOUNTING ADVISORY

MARK SPENCER

Director/Accounting Advisory Leader
mark.spencer@bdo.co.uk

ACTUARIAL

ROB MURRAY

Partner & Head of Actuarial
rob.murray@bdo.co.uk

SANTIAGO RESTREPO

Director
santiago.restrepo@bdo.co.uk

TAX

THOMAS TO

Director
thomas.to@bdo.co.uk

CORPORATE FINANCE

ADAM WHISTANCE

Director & Head of Insurance M&A
adam.whistance@bdo.co.uk

OLADIPO OYE-SOMEFUN

Director
oladipo.oye-somefun@bdo.co.uk

FORENSICS

RICHARD CAMERON-WILLIAMS

Partner
richard.Cameron-Williams@bdo.co.uk

OUTSOURCING

ROBERT HUTCHINGS

Director
Robert.Hutchings@bdo.co.uk

FOR MORE INFORMATION:

ALEX BARNES

+44 (0)20 7651 1213
alex.barnes@bdo.co.uk

CHARLES PORTSMOUTH

+44 (0)20 7651 1428
charles.portsmouth@bdo.co.uk

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