

August Newsletter
Issue 8/2009

Editorial

So here we have another case of FSA enforcement action against a Lloyd's broker, where we need to note the facts and then try and read between the lines to decide if anything needs to be done. The issue for some small brokers may well be firstly how to dispose of that incorrect insurance documentation appropriately rather than just chucking it in the bin. Secondly and perhaps more fundamentally is the FSA pointing firms towards them all having to have a 'clear desk policy'? The judgement doesn't mention the phrase but the FSA has already highlighted it elsewhere as good practice. Therefore don't be surprised if you get a visit this will certainly be on the agenda.

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Further information on the issues in this newsletter, or any other issues which concern your business, can be obtained from
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Changes to the FSA's Approved Persons regime

The FSA has confirmed an extension of the approved persons regime for those that perform a 'significant influence' function at firms.

In its supervisory enhancement programme the FSA stated that it would place greater emphasis on the role of senior management, including non-executive directors. The policy statement issued sets out changes to the approved persons regime which improves FSA's approach to 'significant influence' functions by ensuring that those likely to exert a significant influence on a firm fall within the scope of the approved persons regime.

In particular the FSA has extended the scope and application of CF1 (director function) and CF2 (Non-Executive Director) to include those persons employed by an unregulated parent undertaking or holding company, whose decisions or actions are regularly taken into account by the governing body of a regulated firm.

Code of good conduct for brokers

BIPAR, the European federation of Insurance Intermediaries in its July newsletter has highlighted that the French association of insurance brokers has drawn up a Code of Good Conduct that governs relationships between wholesale brokers and direct brokers regarding information and advice requirements. Wholesale brokers are considered by French law as direct brokers and are therefore subject to the same professional requirements. The Code has been

introduced to clarify the situation. It specifies that a wholesale brokers' responsibility with regard to the information and advice obligation can only be limited as they are never in contact with the final consumer. However it must provide direct brokers with all the necessary information so that they can meet their obligations. Unfortunately the Code is only available in French!

Lloyd's business in Switzerland

Earlier in the year Lloyd's issued a market bulletin which advised that a draft Insurance Contract Law had been released for consultation in Switzerland.

The bulletin summarised the draft law by providing information about the key provisions and potential impact upon the market as well as the general essence of the law, including the proposed approach to commission and fees. The bulletin also requested feedback from market participants on these issues in order for Lloyd's to understand the impact upon the market's business and to assist Lloyd's in formulating a response to the consultation.

As a result of feedback from the market and a detailed analysis of the draft law the Lloyd's submission will focus upon the following:

- Broker remuneration
- Insurance intermediary activity - broker / agent separation
- The lack of differentiation between commercial and personal lines business

- The increase in requirements for third party liability claims

The Lloyd's response will be submitted by the deadline of 31 July 2009.

FSA fines HSBC Insurance Brokers Ltd

The FSA has fined three HSBC firms over £3 million for not having adequate systems and controls in place to protect their customers' confidential details from being lost or stolen. These failings contributed to customer data being lost in the post on two occasions.

HSBC Life UK Limited was fined £1,610,000, HSBC Actuaries and Consultants Limited was fined £875,000 and HSBC Insurance Brokers Limited was fined £700,000.

HSBC Insurance Brokers Ltd (HSBC) failed to have in place adequate and effective procedures, guidance and resources to ensure that:

- (1) customer data sent to third parties on portable electronic media (e.g. CDs, floppy disks and USB devices) was secure in the event that the data was lost or intercepted;
- (2) customer data sent to third parties in hard copy form was sent securely;
- (3) customer data kept in its offices was at all times secure from the risk of internal fraud or theft; and
- (4) an appropriate due diligence process was followed prior to contracting services to third parties such as waste disposal firms.

It failed to properly assess these risks and to implement robust systems and controls to deal with

the increased risk that its business could be used for a purpose connected with financial crime and exposed its customers to the risk of being victims of financial crime.

The weak controls surrounding data security resulted in staff practices that placed customer data at risk of loss or theft in that the firm:

1) sent unencrypted electronic media (such as CDs) containing significant amounts of confidential customer data to third parties through the post or by local courier services;

(2) notwithstanding that access to the firm's offices was securely restricted, routinely kept customer data on open shelving or in cabinets which were unable to be locked; and

(3) entered into contracts with third parties such as confidential waste disposal firms without explicitly ensuring that appropriate data security arrangements were in place.

The FSA considered these failings to be particularly serious because:

- (1) during the relevant period HSBC had over 65,000 customers, most of whom were companies in the UK. It handled customer data relating to the individuals associated with a number of personal and group insurance policies the firm arranged for its customers. These individuals are entitled to rely on the firm to take reasonable care to ensure the security of customer data entrusted to it. The failure to implement appropriate data security controls had the potential to expose these individuals to the risk of identity theft and financial loss; and

- (2) the failures occurred following a period of heightened awareness of financial crime issues as a result of government initiatives, increasing media coverage and an FSA campaign about the importance of financial crime within the financial services sector. Further, HSBC was aware that data security and the associated risks of fraud and identity theft were increasing problems for the financial services industry but failed to take sufficient steps within the relevant period to ensure that all of its data security procedures within its businesses were adequate and robust enough to prevent customer data being mislaid and potentially released into the public domain.

FSA's 'on the grapevine' – reliance on IT systems for data security

The FSA is reminding small firms that they should not rely too heavily on IT systems for their data security. Firms should not forget the human factor. They need to think about the office and its surroundings and how easy it would be to get access to information about the business and their clients. Also many small firms have to buy services from another company. If work is outsourced firms should check that the third party suppliers vet their employees or have their own adequate security arrangements in place.