

The FCA's approach to the review of Part VII insurance business transfers (FG18/4)

The Financial Conduct Authority ("FCA") has issued its [final guidance](#) on its approach to the review of insurance business transfers under Part VII ("**Part VII Transfers**") of the Financial Services and Markets Act 2000 ("**FSMA**").

Alongside the Prudential Regulation Authority ("**PRA**"), the FCA plays an "*active role*" in the review process. This guidance sets out its key considerations and general expectations when reviewing a Part VII Transfer, which can be summarised as follows:

- **Initial Considerations** – this Chapter outlines some factors that firms should consider prior to contacting the FCA, and includes discussion of the information firms will need to provide in advance of the pre-application meeting. The FCA emphasises the importance both of their involvement at the outset of any proposed transfer as well as of the continued process of collaboration.
- **Independent Expert** – this Chapter highlights the key factors the FCA will look at when consulting with the PRA as to the suitability of an Independent Expert ("**IE**"). Crucially, an IE must be able to demonstrate (i) independence, and (ii) sufficient skill, experience and resources.

In assessing independence, the FCA will look at an IE's previous and agreed future relationship with the firm, including any previous insurance business transfers they have produced reports in relation to, any consultancy arrangements and other potential conflicts of interest.

On the sufficient skill, experience and resources consideration, the FCA expects firms to provide detailed information and documentation to support their IE nomination. In particular, the FCA looks for specific evidence of relevant experience and an ability to allocate sufficient resource to consider all relevant issues adequately.

- **Overview of the FCA's approach** – this Chapter includes discussion of the FCA's approach to providing views or comments on a transfer. It includes particular detail on the matters the FCA will consider and comment on in order to draft its reports for the Court.

One of the FCA's key objectives is securing an appropriate degree of protection for consumers. As such, it will consider the business rationale for any scheme with a view to ensuring that any changes that may have an adverse impact on policyholders have been considered and offset with "*...mitigating or counteracting proposals*".

In relation to objections, the FCA is clear in its guidance that it will "*...consider in detail*" objections raised by policyholders, how the firm has addressed such objections and how the firm proposes to set out for the Court the representations of policyholders who believe they may be adversely affected.

- **Key documentation** – namely, the scheme document, the form of the IE report, the communications strategy and applications for dispensations from the transfer regulations.

In its guidance, the FCA notes that it has "*...a particular interest*" in some parts of the scheme document. The three C's – clarity, continuity and changes – are the specific points which the FCA will have in mind when conducting its review. The FCA highlights the importance of clarity as to the business and liabilities being transferred – there should be no ambiguity or uncertainty in the language used and the wording should match the commercial intention; on the issue of continuity, the FCA notes that expects to see a "*standard clause*" included in the scheme document to the effect that all proceedings that are on-going, pending, threatened or in contemplation against the transferee will continue after the transfer; and on changes to the scheme document, the FCA draws a distinction between "*...minor and technical amendments*" that can be made without returning to Court, and changes that require discretion, and therefore will likely require Court approval.

On the form of the IE report, the FCA notes the requirement for the PRA to consult it before providing its approval. The FCA conducts its review from the perspective of a policyholder, therefore there is an expectation that the report is "*...easily readable and understandable*". Notably, the guidance identifies that reports: "*...often lack detailed analysis, critical review or reasoning to support a conclusion that there is likely to be no material adverse effect on policyholder groups.*" Firms are therefore urged to ensure that detailed factual descriptions are supported by sufficient analysis. Over-reliance on the assessments of the applicant by IEs is also identified as an area of concern. The FCA looks for evidence that IEs have challenged the information provided to reach their "*...own conclusions on matters*".

The communications strategy, specifically the requirement to notify policyholders and advertise the scheme, is described as a "*...fundamental protection*". The FCA expects firms to recognise this when determining their approach to policyholder communications, and IEs to include consideration of the proposed approach in their report. In its guidance, the FCA states that their expectations of the communications strategy form a "*...large part of our overall conduct consideration*". As such, the guidance provides significant detail on the various components – from content to translation – that the FCA will focus on in its review of this aspect. Considerable emphasis is placed on the content point, noting that communications must be "*... clear, fair and not misleading*".

- **Dispensations** – the FCA recognises that there will be occasions where firms are "*unable or unwilling*" to notify everyone who falls under the banner of policyholder. This final Chapter of the guidance provides further insight into the approach the FCA will take when judging whether or not to object to an application for dispensation from the transfer regulations. It emphasises the need for "*...adequate reasoning and evidence*" to be provided in support of any such application. This assessment will include a number of considerations – including, though not limited to, impossibility, practicality and proportionality. One example to note - the FCA states that dispensations based on the disproportionality of costs of notification or advertising are likely to be challenged where the FCA deems that the applicant has not shown enough effort to estimate these costs. The guidance also includes discussion of *The Aviva Judgment*¹ which provides a starting point for assessing dispensation requests. The various factors discussed in Norris J's judgment are critical to the FCA's assessment of whether or not a dispensation is suitable in the circumstances.

¹ Re Aviva International Insurance Limited [2011] EWCH 1901 (Ch.).

Key changes to the guidance following consultation (closed August 2017)

As further detailed in the [summary of feedback](#), the majority of responses received to the consultation were supportive of the FCA's effort to clarify its approach. The FCA dismissed some responses as out-of-scope or too focused on certainty, noting that:

"... this guidance is intended to provide high-level information and examples to help firms understand our expectations..."

A number of changes were made to the guidance to give greater clarity on points raised by the consultation. A selection of the amendments can be summarised as follows:

- **Comply or explain** – the FCA has amended the introductory statement to clarify that the purpose of the guidance is to help firms identify areas of the transaction that differ from the expectations as early on in the process as possible to avoid delays closer to the Court dates, not to adopt a "comply or explain" approach. Examples given in the guidance are therefore illustrative, not binding.
- **Competition** – the FCA has clarified its guidance on the level to which IEs are expected to consider competition issues in light of concerns by some respondents that the initial guidance expected an inappropriate level of expertise from IEs on such matters. IEs are required to *"...highlight if there are competition-related matters which could affect policyholders"*.
- **Future changes to the Scheme** – in response to queries relating to what exactly might trigger the requirement to involve the regulators and/or the Court when making changes to the scheme document, the FCA has clarified its guidance on the types of changes that would require a return to Court.
- **Definition of policyholder** – a number of respondents queried the FCA's definition of policyholder, noting that it has been interpreted too broadly. They noted in particular that the definition should not be interpreted so as to extend to, for example, employees under an employer's liability policy. The FCA states in its summary that it *"...is not necessary for us to accept these arguments given the uncertainty of the scope of the definition of policyholder"*. It urges applicants instead to try, where appropriate, to apply for dispensations which could achieve the same outcome.