

Chapter 13

Financial Resources Requirements for Personal Investment Firms

13.1 APPLICATION, GENERAL REQUIREMENTS AND PROFESSIONAL INDEMNITY INSURANCE REQUIREMENTS

Application

- 13.1.1 **R** This chapter applies to a *firm* which is a *personal investment firm*.
- (2) [deleted]
- (3) [deleted]

Purpose

- 13.1.2 **G** This chapter amplifies *threshold condition* 2D (Appropriate resources) by providing that a *firm* must meet, on a continuing basis, a basic solvency requirement and a minimum capital resources requirement. This chapter also amplifies *Principles* 3 and 4 which require a *firm* to take reasonable care to organise and control its affairs responsibly and effectively with adequate risk management systems and to maintain adequate financial resources by setting out capital resources for a *firm* according to the *regulated activity* or activities it carries on.
- 13.1.3 **G** Although financial resources and appropriate systems and controls can generally mitigate operational risk, professional indemnity insurance has a role in mitigating the risks a *firm* faces in its day-to-day operations, including those arising from not meeting the legally required standard of care when *advising on investments*. The purpose of the *rules* in this section is also to ensure that a *firm* has in place the type, and level, of professional indemnity insurance necessary to mitigate these risks.

General capital resources and solvency requirements

- 13.1.4 **R** A *firm* must at all times:
- (1) have and maintain capital resources at least equal to its relevant capital resources requirement; and
- (2) be able to meet its liabilities as they fall due.

Capital resources: general accounting principles

- 13.1.4A **R** Unless a *rule* provides otherwise, a *firm* must:
- (a) recognise an asset or liability; and
 - (b) measure the amount of that asset or liability, by using the accounting principles it applies in preparing the *firm's* reporting form in (2).
- (2) The accounting principles are referred to in the Notes for completion of the Retail Mediation Activities Return (*RMAR*) (under the heading "Accounting Principles") in ■ SUP 16 Annex 18BG.

Requirement to hold professional indemnity insurance

- 13.1.5 **R** A *firm* must take out and maintain at all times professional indemnity insurance that is at least equal to the requirements in this section from:
- (1) an *insurance undertaking* which is authorised to transact professional indemnity insurance in the *UK*
 - (2) a *person of equivalent status* in:
 - (a) a Zone A country;
 - (b) the Channel Islands, Gibraltar, Bermuda or the Isle of Man.

[Note: articles 10(4) and 10(5) of the *IDD*

- 13.1.6 **R** [deleted]

Comparable guarantee

- 13.1.7 **R**
- (1) A *firm* is not required to effect or maintain professional indemnity insurance if a *bank*, *building society* or an *insurer* provides the *firm* with a comparable guarantee.
 - (2) If the *firm* is a member of a *group* in which there is a *bank*, *building society* or an *insurer*, the *firm's* comparable guarantee must be from that *bank*, *building society* or *insurer*.
 - (3) A comparable guarantee means an enforceable, written agreement on terms at least equal to those required by ■ IPRU-INV 13.1.9R to ■ 13.1.13R, as appropriate.

Relevant income

- 13.1.8 **R** The term "relevant income" in this section refers to all income received or receivable which is commission, brokerage, fees or other related income, whether arising from the *firm's permitted activities* or not, for the last accounting year prior to inception or renewal of the professional indemnity insurance policy ("the policy").

Policy terms

13.1.9 **R** The policy must incorporate terms which are appropriate and must make provision for cover in respect of any claim for loss or damage, for which the *firm* may be liable as a result of an act or omission by:

- (1) the *firm*; or
- (2) any *person* acting on behalf of the *firm* including *employees*, appointed representatives or its other *agents*.

Limits of indemnity

13.1.10 **R** If the *firm* is an *IDD insurance intermediary*, the appropriate minimum *limits of indemnity* per year are no lower than:

- (1) EUR 1,300,380 for a single claim against the *firm*; and
- (2) EUR 1,924,560 in the aggregate.

[Note: articles 10(4) and 10(5) of the *IDD*]

13.1.11 **R** [deleted]

13.1.12 **R** [deleted]

13.1.13 **R** If the *firm* is not an *IDD insurance intermediary*, then the following *limits of indemnity* apply:

- (1) if the *firm* has relevant income of up to £3,000,000, no lower than £500,000 for a single *claim* against the *firm* and £500,000 in the aggregate; or
- (2) if the *firm* has relevant income of more than £3,000,000, no lower than £650,000 for a single claim against the *firm* and £1,000,000 in the aggregate.

13.1.14 **G** [deleted]

13.1.15 **R** If a policy is denominated in any currency other than euros, a *firm* must take reasonable steps to ensure that the *limits of indemnity* are, when the policy is effected (i.e. agreed) and at renewal, at least equivalent to those denominated in euros.

13.1.16 **G** A *firm* should consider whether the overall cover is adequate taking account of 13.1.22G(2) and whether the *firm* should seek additional cover or legal expenses insurance. (Legal defence costs are costs of defence against claims that fall under the terms of the policy.)

13.1.17 **G** The cover provided by the policy should be wide enough to include the liability of the *firm*, its *appointed representatives*, its *tied agents*, *employees*

and its agents for breaches under the *regulatory systems* or civil law. If the *firm* operates outside the *United Kingdom* then the policy should cover other regulatory requirements imposed under the laws of other countries in which the *firm* operates.

Policies providing for more than one firm

13.1.18 **R** If the *policy* provides cover to more than one *firm* then:

- (1) The relevant income for calculating the limits of indemnity is that of all the *firms* named in the policy combined;
- (2) each *firm* named in the policy must have the benefit of the minimum *limits of indemnity* as required in this section; and
- (3) each *firm* named in the policy must notify the *FCA* if the aggregate cover in the policy falls below the minimum *limits of indemnity*.

Limits of indemnity – additional requirements

13.1.19 **R** In addition to the specific requirements in ■ IPRU(INV) 13.1.9R to ■ IPRU(INV) 13.1.13R

, the policy must make provision for the following:

- (1) for a *firm* with relevant income of more than £10,000,000, the aggregate limit identified in the table below:

Relevant income is (£)		Minimum aggregate <i>limit of indemnity</i>
more than	up to	(£)
10,000,000	12,500,000	2,000,000
12,500,000	15,000,000	2,400,000
15,000,000	17,500,000	2,800,000
17,500,000	20,000,000	3,150,000
20,000,000	25,000,000	3,800,000
25,000,000	30,000,000	4,250,000
30,000,000	35,000,000	4,500,000
35,000,000	40,000,000	4,750,000
40,000,000	50,000,000	5,500,000
50,000,000	60,000,000	6,000,000
60,000,000	70,000,000	6,750,000
70,000,000	80,000,000	7,250,000
80,000,000	90,000,000	7,750,000

90,000,000	100,000,000	8,500,000
100,000,000	150,000,000	11,250,000
150,000,000	200,000,000	14,000,000
200,000,000	250,000,000	17,000,000
250,000,000	300,000,000	19,750,000
300,000,000	n/a	22,500,000

(2) full retroactive cover in respect of the kinds of liabilities described in ■ 13.1.9R for claims arising from work carried out by the *firm*, or on its behalf, in the past; and

(3) cover in respect of *Ombudsman* awards made against the *firm*.

Limitations

- 13.1.20 **R** The policy must not be subject to conditions or exclusions which unreasonably limit its cover.
- 13.1.20A **R** The policy must not limit cover which would otherwise be provided by the policy where:
 - (1) any of the following default:
 - (a) the *firm*; or
 - (b) a *person* or fund relevant to a potential claim; or
 - (2) a *person* other than the *firm* is entitled to make a claim on the policy.
- 13.1.20B **R**
 - IPRU(INV) 13.1.20AR does not limit the generality of the scope of ■ IPRU(INV) 13.1.20R.
 - (2) In ■ IPRU(INV) 13.1.20R and ■ IPRU(INV) 13.1.20AR, “limit cover” includes limiting by exclusion, by policy excesses or otherwise.
 - (3) In ■ IPRU(INV) 13.1.20AR, “default” means becoming:
 - (a) *in default*;
 - (b) insolvent or likely to be unable to satisfy claims against it; or
 - (c) the subject of one or more of the proceedings listed in ■ COMP 6.3.3R in the *United Kingdom* (or of equivalent or similar proceedings in another jurisdiction) whether or not a determination under ■ COMP 6.3.3R has been made.
- 13.1.20C **R** The policy’s terms must include a statement confirming that the policy complies with ■ IPRU(INV) 13.1.20AR.

13.1.20D G

- (1) An example of a *person* or fund relevant to a potential claim (see ■ IPRU(INV) 13.1.20AR(1)(b)) is a fund the *firm* advised its *customers* to invest in.
- (2) An example of a *person* entitled to make a claim under the policy (see ■ IPRU(INV) 13.1.20AR(2)) is:
 - (a) a *customer* of the *firm* or related *person* by virtue of the Third Parties (Rights Against Insurers) Act 2010; or
 - (b) the *FSCS*.
- (3) One of the purposes of ■ IPRU(INV) 13.1.20AR(2), taken with *COMP*, is that a claim on the policy by the *FSCS* is treated as each of the claims the *FSCS*'s claim represents, taken separately. For example, the *FSCS* may make a claim on the policy in relation to each claim under (2)(a) as a result of assignment.

Exclusions

13.1.21 R

The policy must not:

- (1) exclude any type of business or activity that has been carried out by the *firm* in the past or will be carried out by the *firm* during the time for which the policy is in force; or
- (2) exclude liabilities which are identified or crystallised as a result of regulatory action against the *firm* (either individually or as a member of a *class of authorised persons*);

unless the *firm* holds additional capital resources, in accordance with ■ 13.1.23R.

13.1.22 G

- (1) The *FCA* considers it reasonable for a *firm's* policy to exclude cover for:
 - (a) specific business lines if that type of business has not been carried out by the *firm* in the past and will not be carried out by the *firm* during the life of the policy; or
 - (b) specific *claims* that have been previously notified to the *firm's insurer* and claimed for under another policy.
- (2) The *FCA* does not consider it reasonable for a *firm's* policy to treat legal defence costs cover as part of the *limits of indemnity* if this reduces the cover available for any individual substantive claim.

Additional capital resources - exclusions

13.1.23 R

The amount of additional capital resources that a *firm* must hold as a result of an exclusion under ■ IPRU-INV 13.1.21R must be calculated by referring to the *firm's* relevant income in the following table:

Relevant income £000s	Minimum additional capital resources
more than	£000s
up to	£000s

(Notes 1 and 2)		
0	100	5
100	200	12
200	300	18
300	400	21
400	500	23
500	600	25
600	700	27
700	800	28
800	900	30
900	1,000	31
1,000	1,500	37
1,500	2,000	42
2,000	2,500	46
2,500	3,000	51
3,000	3,500	55
3,500	4,000	59
4,000	4,500	63
4,500	5,000	67
5,000	6,000	73
6,000	7,000	79
7,000	8,000	85
8,000	9,000	90
9,000	10,000	95
10,000	100,000	95y
100,000	n/a	950

Note 1 - For *firms* with relevant income of more than £10m but up to £100m value y is calculated by relevant income/ £10m.

Note 2 - The calculation of a *firm's* capital resources is set out in sections IPRU-INV 13.13 to 13.15.

13.1.24

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The *firm* should hold additional capital resources in excess of those minimum amounts set out in the table in 13.1.23R where the required amounts of

additional capital resources provide insufficient cover, taking into account the *firm's* individual circumstances.

Excess level

13.1.25 **R** The policy must not make provision for payment by the *firm* of an excess on any claim of more than £5,000, unless the *firm* holds additional capital resources, in accordance with 13.1.27R.

13.1.26 **R** The reference to "excess" is to the highest excess level required to be paid under the policy unless that excess relates to a type of business that has not been carried out by the *firm* in the past. In those circumstances, the reference is to the next highest excess level required by the policy applicable to a type of business that has been carried out by the *firm* in the past.

Additional capital resources - excess

13.1.27 **R** The amount of additional capital resources that a *firm* must hold where the policy's excess on any claim is more than £5,000 must be calculated by referring to the *firm's* relevant income and excess obtained in the following table:

All amounts are shown in £000s (Notes 1 and 2)

Relevant income is		Excess obtained, up to and including												
more than	up to	5	10	15	20	25	30	40	50	75	100	150	200+	
0	100	0	4	7	9	12	14	18	21	28	34	45	54	
100	200	0	7	11	14	17	20	25	29	38	46	59	70	
200	300	0	9	14	18	21	24	30	35	45	54	69	82	
300	400	0	11	16	21	24	28	34	39	50	60	77	91	
400	500	0	13	18	23	27	30	37	43	55	66	83	98	
500	600	0	14	20	25	29	33	40	46	59	70	89	105	
600	700	0	16	22	27	31	35	42	49	63	74	94	111	
700	800	0	17	23	28	33	37	45	52	66	78	99	117	
800	900	0	18	24	30	35	39	47	54	69	82	103	122	
900	1,000	0	19	26	31	36	41	49	56	72	85	107	126	
1,000	1,500	0	23	31	37	43	48	57	66	83	99	124	146	
1,500	2,000	0	26	35	42	48	54	64	73	93	109	138	161	
2,000	2,500	0	29	38	46	53	59	71	81	102	121	152	179	
2,500	3,000	0	32	42	51	58	65	78	89	112	132	166	195	
3,000	3,500	0	35	46	55	63	71	84	96	121	142	179	210	

3,500	4,000	0	38	50	59	68	76	90	102	129	152	191	223
4,000	4,500	0	41	53	63	72	80	95	108	137	161	202	236
4,500	5,000	0	43	56	67	76	85	100	114	144	169	212	248
5,000	6,000	0	48	62	73	84	93	110	125	157	185	231	271
6,000	7,000	0	52	67	79	90	101	119	135	169	199	249	291
7,000	8,000	0	56	72	85	97	107	127	144	181	212	265	310
8,000	9,000	0	59	76	90	103	114	134	152	191	224	280	328
9,000	10,000	0	63	80	95	108	120	141	160	201	236	294	344
10,000	100,000	0	63y	80y	95y	108y	120y	141y	160y	201y	236y	294y	344y
100,000	n/a	0	630	800	950	1080	1200	1410	1600	2010	2360	2940	3440

Note 1 - For *firms* with relevant income more of £10m but up to £100m value *y* is calculated by relevant income/ £10m.

Note 2 - The calculation of a *firm's* capital resources is set out in section IPRU-INV 13.13 to 13.15.

Notification requirements

13.1.28

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A *firm* must notify the *FCA* immediately if it becomes aware, or has information which reasonably suggests, that any of the following matters in relation to its professional indemnity insurance has occurred, may have occurred or may occur in the foreseeable future:

- (1) professional indemnity insurance cannot be obtained within 28 days of the inception or renewal date;
- (2) professional indemnity insurance is cancelled;
- (3) the amount of aggregate cover is exhausted;
- (4) the *firm* commences business lines for which it had not obtained cover;
- (5) the *firm* is relying on a policy cover for more than one *firm*; or
- (6) the *firm* is relying on a comparable guarantee provided in accordance with the *rules* in this chapter.

13.1.29

G

- (1) For the purposes of the provisions relating to professional indemnity insurance, "additional capital resources" means readily realisable *own funds* or capital resources under ■ IPRU-INV 13.15.3R, depending on the type of *firm*.
- (2) The *FCA* expects items included in *own funds* or capital resources under ■ IPRU-INV 13.15.3R, depending on the type of *firm*, to be regarded as "readily realisable" only if they can be realised, at any given time, within 90 days.