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Conduct Risk: what is it and what is your role in managing it?

Brandon Horwitz, HSBC Bank plc
and David Morey, PwC

The views expressed are those of the speakers and not necessarily of their employers

Conduct Risk

- Financial Conduct Authority (FCA) views Conduct Risk through prism of their objectives:
  - Consumers get financial services and products that meet their needs from firms they can trust.
  - Markets and financial systems are sound, stable and resilient with transparent pricing information.
  - Firms compete effectively, with the interests of their customers and the integrity of markets at the heart of how they run their business.
- Conduct Risk = Risk of not achieving these objectives

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Actuarial Risk

- General definition of Actuarial Risk = Risk of not achieving objectives of client / firm / product
- Examples of objectives:
  - DB Pension fund has enough money to pay all members’ benefits
  - Investment product delivers performance in line with stated objective
  - Insurance product pays out claims to customers when due
- Actuarial Risk = Conduct Risk?

Managing Risk

- Actuaries have always specialised in managing risks
- Same examples:
  - Designing DB Pension investment & contribution strategy to maximise chance of there being enough money to play all members’ benefits
  - Designing and managing investment strategies so that investment products deliver performance in line with stated objective
  - Pricing products and managing insurer reserves to ensure sufficient funds to pay out claims to customers when due
- Does this cover all relevant Conduct Risks?

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What about Sales of Products?

- Actuaries have always designed and managed products for consumers
- Relatively less involvement in sales strategy and associated controls
- High profile issues in recent years involved mis-selling, resulting in costly remediation / fines for firms
- Conduct Risk crystallised = Solvency Risk ...

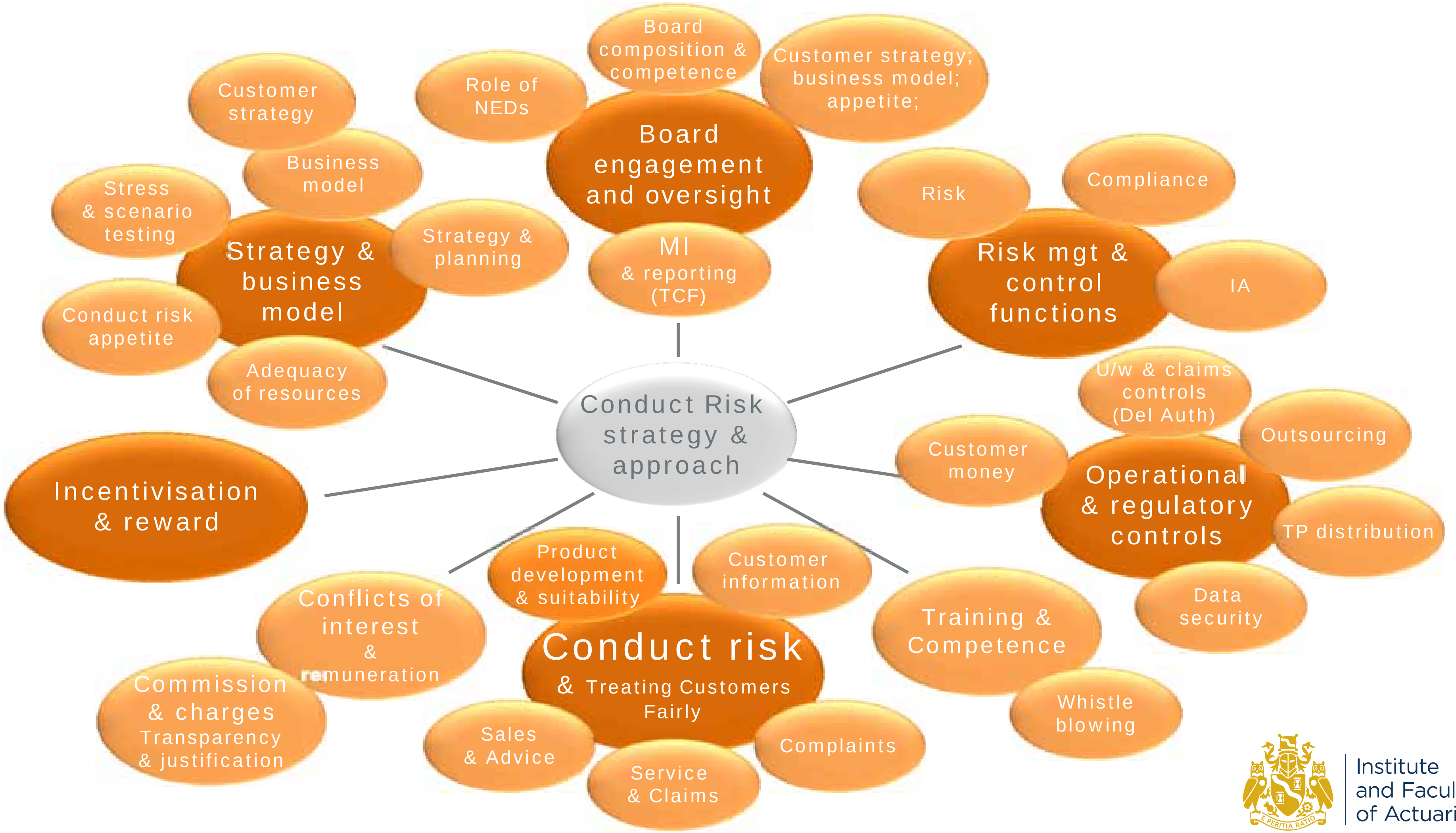
The old TCF model

- Recent conduct risk issues (examples)
  - Case study 1: £15bn+ compensation bill for PPI market
  - Case study 2: CPP fined £10.5m and to pay redress of £14m
  - Case study 3: Restriction to sale of add-ons for a motor distributor
  - Case study 4: Large-scale mis-sale of interest rate swaps to SMEs
- Common issues in the FS markets
  - Product design; Terms & conditions; Mis-selling; Charging practices; Servicing standards; Complaints handling; Incentivisation schemes & pressure selling
- Does the old TCF model work?

New FCA supervision regime

- New focus – “Conduct Risk” & “market integrity”
- Change in approach Reactive → Pre-emptive
- “Intensive and intrusive” supervision
  - Business model analysis; Additional information & reporting
  - Increasing focus on thematic & event-driven visits;
    Deep-dives & file reviews; CEO certification letters
  - Continuing focus on “outcomes”
  - Stronger intervention & enforcement
- New intervention measures, earlier in product life cycle
  - E.g. Product bans; Trading restrictions; Permission requirements
- Already reflected in visits & outcomes
  - RMPs; S166s & “near S166s”; Attestation by accountable executives

Evidencing conduct risk management



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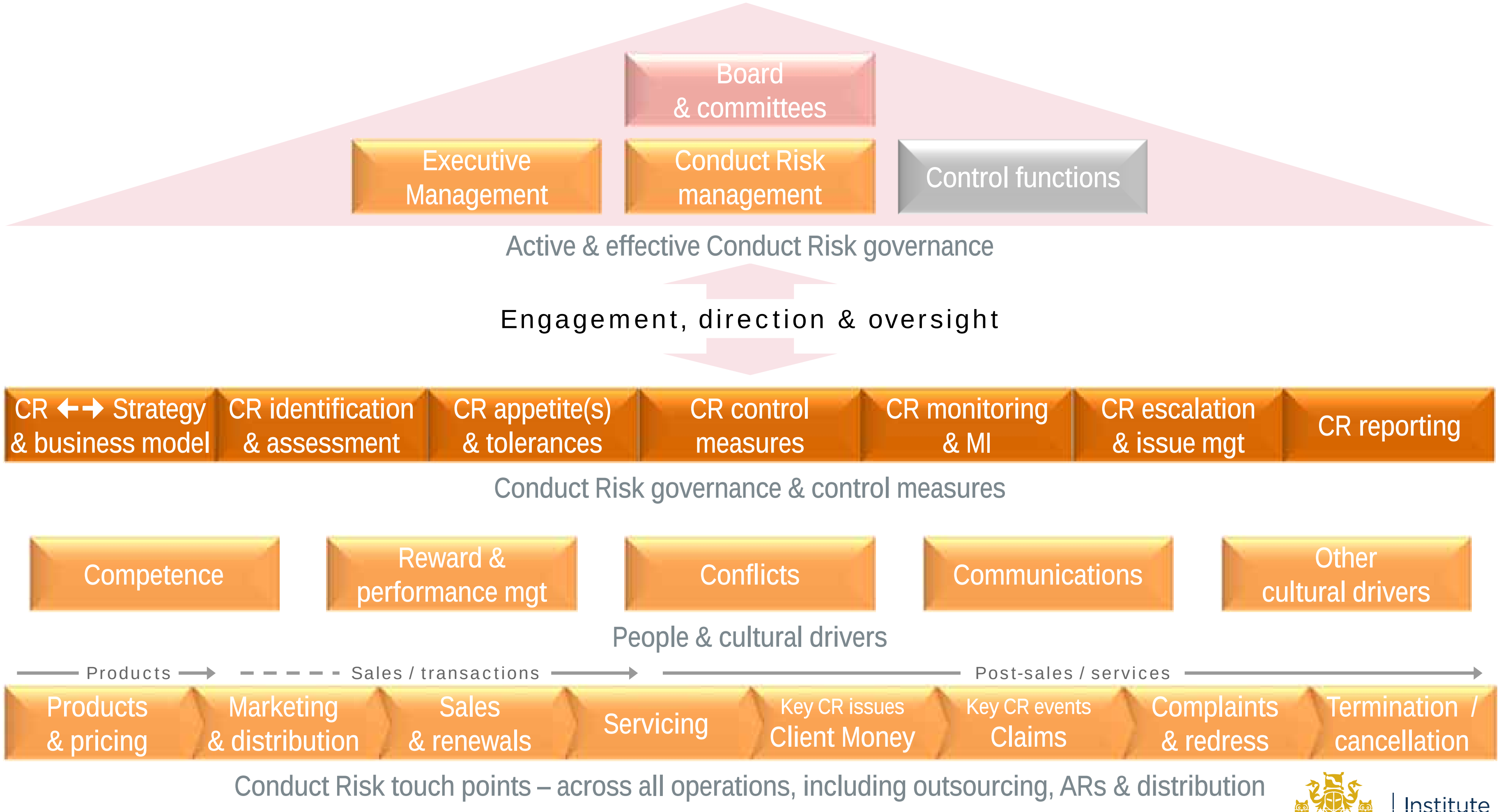
Conduct risk framework - illustration



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Questions

- Is Conduct Risk on your / your firm's agenda?
- Are you involved and if so how?
- What does a good Conduct Risk management framework look like?
- Why should you be concerned about Conduct Risk?
- What are the key obstacles to increasing attention on Conduct Risk?
- How should Conduct Risk appetite be measured?

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