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REGULATORY

UK: Consumer Duty – FCA publishes feedback and Dear CEO letter

Following its policy statement PS22/9 and finalised guidance FG22/5 on the Consumer Duty,[1] the FCA has recently published more guidance on this area in the form of (i) feedback for all firms and (ii) a Dear CEO letter to firms in the general insurance and pure protection sectors.

It is important for firms to consider the content of the feedback (and letter, if applicable) as the FCA has stated that it will focus its supervision on, and may ask for evidence of, how firms have made consequential changes to their business.

Feedback for firms

The FCA has published feedback on its review of firms' implementation plans in relation to the Consumer Duty. The review considered a range of factors in respect of firms' approach to embedding the Consumer Duty within their businesses.

The FCA acknowledged that many firms have understood and embraced the shift to focussing on consumer outcomes, established extensive programmes to embed the Consumer Duty and engaged with the requirements. However, the FCA noted that some firms are behind in planning for the Consumer Duty and may struggle to meet the implementation deadlines or embed it effectively throughout their business.

Dear CEO letter

The FCA has published a Dear CEO letter to firms in the general insurance (GI) and pure protection (PP) sectors to help them implement and embed the Consumer Duty effectively. The letter provides specific guidance to those firms and expands upon the separate feedback provided to all firms.

The letter also sets out further information and examples as to how the Consumer Duty applies to firms in the GI and PP sectors.

Key areas for focus – all firms

In both its feedback and the Dear CEO letter, the FCA has identified three key areas for all firms to focus on for the remainder of the implementation period:

1. **Effective prioritisation:** Implementation plans should be clear as to the basis for prioritising certain areas of embedding work. Firms should make sure that the areas of their business which will have the biggest impact on customer outcomes are prioritised.
2. **Embedding the substantive requirements:** Firms should carefully consider the substantive requirements of the Consumer Duty and ensure that they are making the changes necessary for customers to receive relevant communications and updates, be offered products and services that they actually need and get the right support when they need it. In particular, many implementation plans for GI and PP firms were found to be high-level in nature and lacking sufficient granularity.
3. **Working with other firms:** This includes sharing information (both with other firms in the distribution chain and where firms outsource the delivery of services to third parties), to ensure that all firms and any third-party arrangements are able to deliver good customer outcomes. This is an area in which some firms (in particular, manufacturers and distributors) are falling behind currently and need to accelerate their work.

The FCA's feedback also contains examples of good practice, and areas of improvement, for firms to improve their implementation approach.

Key areas for focus – GI and PP firms

In its Dear CEO letter, the FCA has identified three key areas for GI and PP firms to focus on for the remainder of the implementation period:

1 Please refer to our September 2022 insurance bulletin article titled: "FCA introduces new Consumer Duty".

1. **Effectiveness of product governance arrangements:** Firms should review whether their products and services are delivering fair value. In particular, they should ensure that their product governance arrangements evidence that their products offer fair value to retail customers.
2. **Effectiveness of communication with customers:** Firms should ensure that customers receive timely information, and in a format that will enable them to make informed decisions on whether a product meets their needs. Firms must test, monitor and adapt communications to support understanding and good outcomes for customers. Firms should apply the same standards in ensuring their communications are delivering good customer outcomes, as they do in ensuring their communications generate sales and revenue.
3. **Claims processes and outcomes:** Firms should ensure they support customer understanding and deliver good outcomes throughout the claim journey, through timely and appropriate communications. Customers should be at the centre of the claims process, so that unreasonable delays to claims processing are avoided and fair claims settlements are made.

Annex 2 to the letter contains more detail on these issues and how they apply to firms in the GI and PP sectors, including relevant examples of good and poor practice.

Looking ahead

Firms must implement, and embed effectively, the Consumer Duty in line with the following deadlines:

- **End of April 2023:** manufacturers should have completed all reviews necessary to meet the outcome rules and shared necessary information with their distributors.
- **31 July 2023:** the Consumer Duty will come into force for new and existing (open to sale or renewal) products and services.
- **31 July 2024:** the Consumer Duty applies to closed products and services.

In implementing and embedding the Consumer Duty, firms should ensure that they consider the key areas outlined in the FCA's feedback (and Dear CEO letter, if applicable) – the FCA has stated that those areas are likely to be the primary focus of its future supervisory work and it may ask for evidence of how firms have made the necessary changes to their business in light of the feedback (and letter).

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EU: EIOPA aims to strengthen oversight of third country governance arrangements with supervisory statement

On 3 February 2023, the European Insurance and Occupational Pensions Authority (EIOPA) published a supervisory statement (SS) (EIOPA-22/362) aiming to strengthen supervision and monitoring of EU insurance undertakings and intermediaries when using governance arrangements in third countries to perform functions or activities.

The SS emphasises that firms should ensure that third country branches primarily serve the market in which they are located and do not act as "outposts" for firms which in turn "become empty shells". EIOPA considers that, by strengthening their supervision and guidance, firms will retain sufficient levels of corporate substance within the EEA that is proportionate to the nature, scale and complexity of their business.

EIOPA states that sufficient levels of corporate substance include:

1. an appropriate presence of administrative, management or supervisory board members and key function holders in the HQ of a company who dedicate sufficient time to fulfil their duties within the third country establishment to guarantee effective decision-making and risk management;
2. that regulated function or activities should not be structured in a way that they impair the ability of the supervisory authorities to monitor the compliance of a Firm; and
3. that a firm should not be "disproportionately dependent" on the arrangement in a third country branch for its activities which are based in the EU.

With the above in mind, firms with third country branches need to ensure that they have sufficient corporate substance within the EEA and that they can show that it is proportionate to the nature, scale and complexity of their business. We have been advising a number of EEA firms with UK branches on this issue and related matters, with the aim of ensuring that such firms can continue to undertake their business in the UK in a manner which achieves their commercial aims.

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"After careful consideration, the Court held that the clause did apply although the decision considered and raised various complex questions which are likely to require further scrutiny from the higher English courts. "

DISPUTES

"Plane" English: High Court upholds no-assignment clause to prevent transfer to insurer

In the recent important case of *Dassault Aviation SA v Mitsui Sumitomo Insurance Co Ltd*[1] the English Commercial Court had to consider the thorny issue of whether a no-assignment clause in a sale contract for two aircraft applied when the insured's rights had been assigned to its insurer under an insurance policy. After careful consideration, the Court held that the clause did apply although the decision considered and raised various complex questions which are likely to require further scrutiny from the higher English Courts.

Dassault Aviation SA as seller (**Dassault**) entered into a sale contract dated 6 March 2015 with a buyer (the **Sale Contract**). The Sale Contract was subject to English law and provided that Dassault would construct and supply two Dassault Falcon surveillance aircraft and associated parts and services to the buyer. Separately, the buyer contracted with the Japanese Coast Guard to supply the aircraft to them.

Clause 15 of the Sale Contract was headed "Assignment-Transfer". Clause 15 provided, with limited express exceptions, that the parties were prohibited from transferring or assigning rights, as follows:

".. this Contract shall not be assigned or transferred in whole or in part by any Party to any third party, for any reason whatsoever, without the prior written consent of the other Party and any such assignment, transfer or attempt to assign or transfer any interest or right hereunder shall be null and void without the prior written consent of the other Party....".

The buyer obtained an insurance policy (the **Policy**) from Mitsui Sumitomo Insurance Co Ltd (**the insurer**) (without informing Dassault) covering its liability to pay damages to the Coast Guard if the aircraft were delivered late. The Policy was subject to Japanese law.

Delivery of both aircraft was considerably delayed and the Japanese Coast Guard did claim damages from the buyer, which then claimed an indemnity for those damages under the Policy. The insurer accepted and paid the indemnity.

Under insurance policies subject to English law (and the law of many other jurisdictions), the principle of subrogation enables an insurer to "step into the shoes" of its insured when an insurer pays an indemnity to an insured and allows the insurer to pursue any third party which was responsible for the insured loss. The recovery action then proceeds in the name of the insured, although in practice it is usually directed by insurers, given that the insured is already indemnified. However, in this case, the Policy was subject to Japanese law. Under Article 25 of the Japanese Insurance Law, the insured's rights are automatically assigned to the insurer by operation of law, when an insurer indemnifies its insured.

The insurer sought to pursue Dassault for damages for late delivery in its capacity as assignee of the buyer's rights. The Sale Contract provided for ICC arbitration. Dassault argued that the arbitral tribunal had no jurisdiction to hear the matter on the ground that the buyer had breached the Sale Contract, which prohibited assignment. However, Dassault's argument was unsuccessful and the majority of the tribunal held (with Simon Crookenden KC dissenting) that it did have jurisdiction over the matter. Dassault then made an application to the English Commercial Court under section 67 of the Arbitration Act 1996 to set aside the partial award. Section 67 allows parties to challenge an award on the ground that an arbitral tribunal lacked "substantive jurisdiction".

1 [2022] EWHC 3287 (Comm),

Judgment

The case was heard by Mrs Justice Cockerill in the Commercial Court. The Court was required to decide whether the contractual no-assignment clause applied to automatic or involuntary assignments.

The Court considered a series of previous English decisions, many somewhat historic and dealing principally with bankruptcy scenarios, which had traditionally been regarded as meaning that contractual prohibitions on assignment do not apply to transfers "by operation of law". However, the Court held that no such general principle exists and the real question is rather whether the transfer truly occurs outside the voluntary control of the transferring party. In this regard, the Court said that it was apt to consider whether there was a sufficient "degree" or "taint" of voluntariness in the transfer. Considering the particular facts of this case, the Court held that the assignment of the buyer's rights to the insurer was a consequence of voluntary acts by the buyer because the buyer had deliberately taken out the insurance policy and submitted an insurance claim.

The Court therefore found in favour of Dassault that the contractual no-assignment clause was effective. Accordingly, the Court held that the insurer was not entitled to bring its arbitration claim against Dassault and the arbitral tribunal had erred in deciding that it had jurisdiction to hear the dispute when it had none. However, the Court accepted that the questions before it were not straightforward and Mrs Justice Cockerill commented that she had *"reached this conclusion with an unusual degree of hesitation"*.

Insurers have been granted permission to appeal. The appeal is expected to be heard during 2023.

Discussion

The case raises important issues for both insurers and policyholders.

For insurers, the case demonstrates that the prospects of insurers recovering potentially large sums from third parties responsible for the loss could stand or fall on what the governing law clause of the policy says (and how subrogation is thereby treated in the relevant jurisdiction). Such a governing law clause could be merely one sentence in a long policy document. For liability insurers, it reiterates the need for careful consideration where possible of commercial contracts entered into by its insureds regarding issues such as assignment, governing law and any contractual provisions about obtaining insurance and risk allocation. Insurers must also consider the implications of the choice of a different governing law for their policy to that of the underlying contract, including in relation to subrogation.

For policyholders, it demonstrates that no-assignment clauses should be drafted as clearly as possible and favour express provision as to what is permitted over general and broad language. The Court commented that *"while the wording is broad, it is not the broadness of sketchy drafting. It has clear wording covering consequences (voidness) and it has limited exceptions"*. Policyholders should therefore take appropriate legal advice to ensure that the wording of such provisions adequately reflects their intentions.

The case is also another example of how the English Courts will, as far as possible, try to give effect to the contractual wording agreed between commercial parties. Whilst also considering the factual matrix and commercial common sense surrounding the Sale Contract, the Court considered in detail the wording of the clause and noted that it had been drafted so as to provide a broad prohibition on assignment *"for any reason whatsoever"*. The Court was therefore anxious not to stray into the territory of public policy considerations, but to uphold the contractual bargain which the parties have struck. It would not *"strain to reach a result which is essentially one of public policy and which does in truth rewrite the parties' agreement"*.

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"The Court of Appeal emphasised that initial impressions can be important when interpreting ambiguously worded contractual provisions. However, as this case illustrates this is not always a helpful approach"

Court of Appeal decides Covid BI claim cannot be heard in England

In *Al Mana Lifestyle Trading LLC & Ors v United Fidelity Insurance Company PSC & Ors*[1], the Court of Appeal has held, overturning a decision by the Commercial Court, that the English court does not have jurisdiction to hear BI claims brought under various multi-risk insurance policies issued in the Middle East. In doing so, the Court of Appeal emphasised that initial impressions can be important when interpreting ambiguously worded contractual provisions. However, as this case illustrates, this is not always a helpful approach given that initial impressions may differ.

Background

The Claimants all form part of the Al Mana Group, which operates in the food, beverage and retail sectors, predominantly in the Middle East and Gulf regions. In May 2021, they commenced English court proceedings, bringing claims under a suite of seventeen multi-risk insurance policies underwritten by the Defendants (the **Policies**). The Claimants sought an indemnity totalling around US $40 million for business interruption losses arising from the COVID-19 pandemic.

The Defendants are insurers headquartered in the United Arab Emirates, Qatar and Kuwait and the Policies were issued in those jurisdictions.

The Defendants challenged the English court's jurisdiction to hear the claims.

Each of the Policies contained the following wording (the **Clause**):

> *"APPLICABLE LAW AND JURISDICTION:*
>
> *In accordance with the jurisdiction, local laws and practices of the country in which the policy is issued. Otherwise England and Wales UK Jurisdiction shall be applied,*
>
> *Under liability jurisdiction will be extended to worldwide excluding USA and Canada."*

The Defendants' case was that, in each policy, the Clause provided for the exclusive jurisdiction of the court of the country in which the policy was issued, with a fallback for English jurisdiction in the event that the local court did not have or would not accept jurisdiction.

The Claimants argued that the Clause gave the party wishing to bring a claim a free choice to bring proceedings either in the local court or in the courts of England and Wales. Alternatively, if that was wrong, the Claimants contended that the jurisdiction of the English and Welsh courts would be available so long as the jurisdiction of the local court was not mandatory under the law of that country.

First instance decision

At first instance, Cockerill J found that the Clause was not exclusive, and permitted proceedings to be brought *either* in the country where the policy was issued (in this case the UAE, Qatar or Kuwait), *or* in the courts of England and Wales.

In analysing the wording of the Clause, the Court emphasised the importance of giving consideration to every word, and of viewing each word in its place in the Clause, rather than in *"the slightly overfocussed context"* of the parties' submissions.

The Court found that there was only one possibility for the applicable law: the relevant local law. The Court also recognised that this was a factor in favour of the Defendants' contention that the courts of the countries where the policies were issued should have jurisdiction. However, ultimately, the Judge agreed with the Claimants that the words *"in accordance with"* could not be seen as synonymous with *"subject to"*; the former is less mandatory and imperative than the latter. The Judge also considered that the use of the word *"otherwise"* in conjunction with *"in accordance with"* suggested a natural balancing which is more suggestive of a non-exclusive jurisdiction clause.

1 [2023] EWCA Civ 61.

Court of Appeal decision

The Court of Appeal, by a 2-1 majority (Andrews LJ dissenting), allowed the Defendants' appeal, finding that the English court did not have jurisdiction to try the Claimants' claims.

The Court agreed with the first instance Judge that the test to be applied was how the words of the Clause would be understood by a reasonable policyholder. Males LJ (with whom Nugee LJ agreed) noted that, in applying this test, first impressions are important, and his strong impression on first seeing the Clause was that the first sentence contained the primary jurisdiction selected by the parties, with a fallback for English and Welsh jurisdiction in the second sentence. That impression was confirmed on a more analytical reading of the Clause.

The Clause made clear that local governing law and practices would continue to apply, even if the English court heard the claim, and this was a powerful factor in favour of the Defendants' argument that the choice of local jurisdiction was intended to be mandatory.

Males LJ considered that in the context of the Clause, the words *"in accordance with"* were imperative and mandatory, and *prima facie*, therefore, the choice of the jurisdiction of the local court would also be mandatory. This was subject to the effect of the second sentence and in particular the use of the word *"otherwise"*. Males LJ's view was that in the context of a jurisdiction clause, the word "otherwise" was more appropriate to introduce a fallback. Males LJ concluded that the fallback of England and Wales would be available only if the local court did not or would not accept jurisdiction. Males LJ did not think it was relevant – as the Claimants had argued – that there were no or very limited circumstances in which the local court would not accept jurisdiction: there was no reason why parties could not agree a fallback jurisdiction without first investigating the likelihood of it being necessary. There was also no need for a single neutral venue where it had not been suggested that the local courts could not handle the claims in an independent, efficient, cost-effective and timely manner.

Dissenting, Andrews LJ indicated that her strong first impression of the meaning of the clause was the opposite to that of Males LJ. Andrews LJ agreed that a key consideration was the meaning of the word *"otherwise"* at the start of the second sentence, but considered that the more natural and obvious interpretation of the Clause was that if, for whatever reason, the proceedings were not brought in the courts of the country where the policy was issued, they must be brought in England and Wales. Andrews LJ was therefore of the view that the first instance decision was correct, and that the Clause should be interpreted as a non-exclusive jurisdiction clause.

Comment

Perhaps even more so now that the first instance decision has been overturned, this case highlights the importance of clearly drafted policy provisions. As the case illustrates, an ambiguously worded (or, as Males LJ put it, *"tersely expressed"*) jurisdiction clause can create a great deal of uncertainty, which in turn can lead to costly and time-consuming jurisdictional disputes arising before the substantive issues can be dealt with. Clearly, this is in the interests of neither policyholders nor insurers.

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