ROUND UP OF REGULATORY DEVELOPMENTS
IN DECEMBER 2019

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WELCOME TO OUR INSURANCE REGULATORY EBULLETIN

Welcome to this edition of our Insurance Regulatory eBulletin, which aims to keep you updated with significant regulatory developments and their implications across the insurance sector.

I wish all our readers a happy and prosperous New Year and we look forward to keeping you informed of regulatory developments throughout 2020. 2019 has seen some significant regulatory developments including the extension of the Senior Managers and Certification Regime (SM&CR) to all financial services firms. Brexit continues to cause some regulatory uncertainty (despite the election result) and may mean that there is more change to come. December saw a focus on operational resilience and the potential effects of climate change by the regulators. Both of these topics will continue to be a focus as we move into 2020.

I hope you enjoy reading this latest update. Please do not hesitate to contact myself or your normal BDO contact if you have any concerns over any matter highlighted in this update.

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EIOPA

EIOPA CALL FOR RESEARCH PROPOSALS – DEADLINE EXTENDED

The shape of future European insurance regulatory focus was reiterated on 10 December, when EIOPA extended its deadline for research proposals relating to informing its ongoing policy and regulatory debates. EIOPA is calling for research proposals addressing open questions on the following topics with a special emphasis on the policy issues.

- Investment allocations of insurers and pension funds
- Liquidity stress testing in the insurance sector
- Early warning systems in insurance
- Systemic relevance of insurance sector and its interlinkages with financial and real sectors
- Economic valuation of insurers' liabilities; best estimate and risk margin.

The deadline for submission of research proposals is extended to 15 January 2020 with outcomes being announced on 28 February.

CONSULTATION ON PROPOSED GUIDELINE ON ICT SECURITY AND GOVERNANCE

On 12 December, EIOPA published a Consultation Paper on its proposed Guidelines on Information and Communication Technology (ICT) security and governance. EIOPA has identified the necessity of developing specific guidance on ICT security and governance in relation to Articles 41 and 44 of the Solvency II Directive arising out of EIOPA's analysis carried out to answer the EC FinTech Action plan, the EIOPA Supervisory Convergence Plan 2018-2019, and related stakeholder correspondence.

The objectives of the Guidelines are to:

- provide clarification and transparency to market participants on the minimum expected information and cyber security capabilities
- avoid potential regulatory arbitrage
- foster supervisory convergence regarding expectations and processes applicable in relation to ICT security and governance as a key to proper ICT and security risk management.

These Guidelines will become the minimum regulatory standards for insurers under Solvency II.

Comments should be received on or before 13 March 2020 with the intention of the Guidelines coming into force in July 2020.

REPORT ON THE USE OF CAPITAL ADD-ONS DURING 2018

On 13 December, EIOPA released a report on the use of capital add-ons by EU regulators or National Competent Authorities (NCAs) during 2018. The analysis is based on 2018 year-end Solvency II data collected under the Solvency II Directive. The report notes that all 31 NCAs reported no changes in the internal process of setting and reviewing capital add-ons for solo undertakings, including solo undertakings that are part of a cross-border group.

The majority of NCAs do not have formal policies in place and the overall use of capital add-ons remains extremely limited. During 2018, eight NCAs set capital add-ons to 21 solo insurance and reinsurance undertakings, and one NCA used it for three groups. These include 10 non-life undertakings, eight life undertakings, two reinsurers and one composite. The UK regulator was the largest user of capital add-ons at solo-level with 12 capital add-ons and all 3 at group level.

Q&A ON REGULATION

On 16 December, EIOPA published new Q&As on the following regulatory issues:

- Answers to (EU) No 2009-138 Solvency II Directive (Insurance and Reinsurance)
- Answers to (EU) No 2015-2450 templates for the submission of information to the supervisory authorities
- Answers to guidelines on reporting and public disclosure

EIOPA REPORT ON INSURERS' ASSET AND LIABILITY MANAGEMENT RELATING TO LIABILITY ILLIQUIDITY

On 16 December, EIOPA published a report on insurers' asset and liability management in relation to the illiquidity of their liabilities. The report supplements information provided in EIOPA's annual report on the long-term guarantee measures and is published in response to a request from the EC in the context of the 2020 Review of Solvency II.

The report provides information on:

- insurance liabilities
- the asset management of insurers
- long-term guarantee measures, including matching adjustment, volatility adjustment, actual yield and dynamic volatility adjustment
- the market valuation of insurance liabilities.

In its analysis, EIOPA investigated the illiquidity of insurance undertakings from two different perspectives:

- a total balance-sheet approach with a focus on how undertakings can hold on to their investments
- a liability perspective that focuses on the predictability of the timing of the cash flows.

EIOPA will use the analysis in this report in its Opinion on the 2020 Review of Solvency II.

EIOPA'S ANNUAL ANALYSIS ON THE USE AND IMPACT OF LONG-TERM GUARANTEES MEASURES AND MEASURES ON EQUITY RISK

On 17 December, EIOPA submitted to the European Parliament, the Council of the EU and the EC, its 2019 and fourth Annual Report on Long-Term Guarantees Measures (LTG) and Measures on Equity Risk. The analysis carried out by EIOPA in the annual reports on long-term guarantees measures and measures on equity risk will serve as a basis for EIOPA's Opinion on the 2020 review of Solvency II.

Similar to previous years' analysis, this year's results show that most of the measures are widely used. 699 (re)insurance undertakings in 22 countries with a European market share of 75% use at least one of the following voluntary measures:

- The matching adjustment
- The volatility adjustment
- The transitional measures on the risk-free interest rates
- The transitional measures on technical provisions
- The duration-based equity risk sub-module

The volatility adjustment and the transitional measure on technical provisions are particularly widely used. The volatility adjustment is applied by 660 undertakings in 22 countries to mitigate the effect of exaggerations of bonds spreads. The transitional measure on technical provisions is applied by 159 undertakings in 11 countries with respect to contracts concluded before the start of Solvency II in order to ensure a smooth transition to the new regime.

The average Solvency Capital Requirement (SCR) ratio of undertakings using the voluntary measures is 235% and would drop to 159% if the measures were not applied. This confirms the importance of these measures for the financial position of (re)insurance undertakings.

Consistent with the trends observed in past years, the availability of long-term guarantee products is mainly stable or decreasing across EEA. In the 2018 report, approximately half of the jurisdictions observed a reduction in the availability of traditional life insurance products with long-term guarantees and an increase in the availability of unit-linked business. All jurisdictions that observed this trend last year, have responded that the trend has continued this year. Overall, national supervisory authorities have observed a decrease in the size and duration of guarantees.

EIOPA SETS OUT KEY FINANCIAL STABILITY RISKS OF THE EUROPEAN INSURANCE AND PENSIONS SECTOR

On 18 December, EIOPA published its December 2019 Financial Stability Report on the (re)insurance and occupational pensions sectors in the European Economic Area. The highlights include:

- The risk of a prolonged low yield environment has intensified over the last 6 months and remains the key challenge for European insurers and pension funds, putting pressure on both solvency positions and long-term profitability
- The combination of weakening economic outlook, concerns over debt sustainability and stretched valuations across financial markets could also give rise to a sudden reassessment of risk premium
- Emerging cyber and climate change related risks continue to demand attention from insurers, pension funds and supervisors
- Interconnectedness with banks and home-bias in investments remain high for European insurers and could lead to potential spill overs of risks from other sectors

EIOPA 2019 CONSUMER TRENDS REPORT

On 19 December, EIOPA) published its 2019 Consumer Trends Report outlining major developments in the insurance and pensions sectors affecting European consumers. Improvements in disclosure practices have been seen and digitalisation remains a broadly noteworthy trend, showing that financial innovations can bring benefits for both insurers and consumers, so long as they are adequately designed and properly implemented.

Accident and health insurance products continue being 'good value-for-money', with the medical expense line of business having the highest claims ratio and the lowest commission rates for non-life insurance products.

However, areas that could cause potential consumer detriment continue being reported, with possible risks for consumers across the product lifecycle. Particular concerns relate to unit-linked, credit life/credit protection and add-on insurance products as well as claims management in motor insurance. We should expect continued regulatory focus on these areas across Europe in the future.

PRUDENTIAL REGULATION

OUTSOURCING AND THIRD PARTY RISK MANAGEMENT – CP30/19

On 5 December, the PRA published a Consultation Paper (CP30/19) setting out its proposals for modernising the regulatory framework on outsourcing and third-party risk management. The proposals are set out in the draft Supervisory Statement (SS) on 'Outsourcing and third-party risk management' in the Appendix to the CP (draft SS) and pursue the following objectives:

- complement the policy proposals on operational resilience in CP29/19 'Operational resilience: impact tolerances for important business services', published simultaneously with this CP
- facilitate greater resilience and adoption of the cloud and other new technologies' as set out in the Bank of England's (the Bank's) response to the 'Future of Finance' report
- implement the European Banking Authority (EBA) 'Guidelines on Outsourcing Arrangements' (EBA Outsourcing Guidelines). The draft SS clarifies how the PRA expects banks to approach the EBA Outsourcing Guidelines in the context of its requirements and expectations. In addition certain chapters in the draft SS elaborate on the expectations in the EBA Outsourcing Guidelines. For instance, chapters 7 (Data Security) and 10 (Business Continuity and exit plans)
- Take into account the draft EIOPA 'Guidelines on Outsourcing to Cloud Service Providers (EIOPA Cloud Guidelines')and EBA Guidelines on ICT and security risk management (EBA ICT Guidelines).

The CP is relevant to all UK banks, building societies and PRA-designated investment firms, insurance and reinsurance firms and groups in scope of Solvency II, including the Society of Lloyd's and managing agents, and branches of overseas banks and insurers.

The consultation closes on Friday, 3 April 2020.

UPDATE TO SOLVENCY II XBRL FILING MANU

On 9 December, the PRA updated the Solvency II XBRL filing manual to help firms and software vendors create XBRL instance documents for Solvency II Pillar 3 and Bank of England Insurance reporting. See the Regulatory Reporting - Insurance sector webpage for the updated filing manual.

THE PRUDENTIAL REGULATORY FRAMEWORK AND LIBOR TRANSITION

On 18 December, the PRA published a letter to the Chair of the Working Group on Sterling Risk-Free Reference Rates. The letter underlines the PRA's view that the need to transition is a critical one for all involved, and firms must take appropriate action now so that they have transitioned to alternative rates ahead of the end of 2021.

BANK OF ENGLAND CONSULTS ON ITS PROPOSALS FOR STRESS TESTING THE FINANCIAL STABILITY IMPLICATIONS OF CLIMATE CHANGE

On 18 December, the Bank of England published a Discussion Paper which sets out its proposed framework for the 2021 Biennial Exploratory Scenario ('BES') exercise. The objective of the BES is to test the resilience of the largest banks and insurers ('firms') to the physical and transition risks associated with different possible climate scenarios, and the financial system's exposure more broadly to climate-related risk.

Whilst climate-related risks will materialise over decades, actions today will affect the size of those future risks. It is therefore important that firms, and other stakeholders such as the Bank, continue to develop innovative approaches to measure climate-related risks before it is too late to ensure resilience to them. The BES will use exploratory scenarios to size these future risks and to explore how firms might respond to them materialising, rather than testing firms' capital adequacy.

The key features of the BES are:

- Multiple Scenarios that cover climate as well as macro-variables: to test the resilience of the UK's financial system against the physical and transition risks in three distinct climate scenarios. These range from taking early, late and no additional policy action to meet global climate goals
- Broader participation: both banks and insurers are exposed to climate-related risks, and the action of one will spill over to affect the other. For insurers, this exercise builds on the scenarios developed for this year's insurance stress test
- Longer time horizon: is needed as climate-related risks crystallise over a much longer timeframe than conventional risks. The BES proposes a modelling horizon of 30 years
- Counterparty-level modelling: a bottom up, granular analysis of counterparties' business models split by geographies and sectors is proposed to accurately capture the exposure to climate-related risks
- Output: the Bank will disclose aggregate results of the financial sector's resilience to climate-related risk rather than individual firms.

The Bank is consulting on the design of the exercise and welcomes feedback on the feasibility and the robustness of these proposals from firms, their counterparties, climate scientists, economists and other industry experts by 18 March 2020. The final BES framework will be published in the second half of 2020 and the results of the exercise will be published in 2021.

OPERATIONAL RESILIENCE

BUILDING OPERATIONAL RESILIENCE: IMPACT TOLERANCES FOR IMPORTANT BUSINESS SERVICES

On 5 December, the Bank of England, PRA and FCA published a shared policy summary and co-ordinated consultation papers on new requirements to strengthen operational resilience in the financial services sector.

Building the operational resilience of firms and Financial Market Infrastructures (FMIs) is a shared priority for the three supervisory authorities. The co-ordinated CPs build on the concepts set out in the operational resilience Discussion Paper published by the authorities last year, addressing many of the proposed policy changes based on the responses we received.

The policy proposals make it clear that firms and FMIs are expected to take ownership of their operational resilience and that they will need to prioritise plans and investment choices based on their impacts on the public interest. If disruption occurs firms are expected to communicate clearly, for example providing customers with advice about alternative means of accessing the service.

Under the proposals, firms and FMIs would be expected to:

- identify their important business services that if disrupted could cause harm to consumers or market integrity, threaten the viability of firms or cause instability in the financial system
- set impact tolerances for each important business service, which quantify the maximum tolerable level of disruption they would tolerate
- identify and document the people, processes, technology, facilities and information that support their important business services
- take actions to be able to remain within their impact tolerances through a range of severe but plausible disruption scenarios.

The PRA published a Consultation Paper (CP29/19) aimed at addressing risks to operational resilience including those arising from the interconnectedness of the financial system, and the complex and dynamic environment in which firms operate. The PRA considers that there is a need for a proportionate minimum standard of operational resilience that incentivises firms to prepare for disruptions and to invest where it is needed.

The CP sets out proposals for:

- PRA rules (Appendix 1 and 2)
- a supervisory statement (SS) (Appendix 3)
- a statement of policy (SoP) (Appendix 4) designed to improve the operational resilience of firms and protect the wider financial sector and UK economy from the impact of operational disruptions. The draft SoP sets out how the PRA proposes to supervise existing policies in the light of the proposed new operational resilience rules and expectations.

This CP is relevant to all UK banks, building societies and PRA-designated investment firms (banks), and UK Solvency II firms, the Society of Lloyd's and its managing agents (insurers). The consultation closes on Friday 3 April 2020.

To complement its policy proposals on operational resilience, the PRA has also published a Consultation Paper (CP30/19) on 'Outsourcing and third-party risk management'. – covered elsewhere in this bulletin.

The FCA also proposed changes to how firms approach their operational resilience. The FCA's Consultation Paper (CP19/32) proposals build on the approach outlined within the Discussion Paper (DP) 'Building the UK Financial Sector's Operational Resilience' from July 2018, expanding on and developing the ideas discussed in the DP based on responses received. The consultation affects banks, building societies, Prudential Regulation Authority designated investment firms, Recognised Investment Exchanges, and Enhanced scope Senior Managers & Certification Regime firms.

The FCA proposes that firms:

- Identify their important business services and document the people, processes, technology, facilities and information that support a firm's important business services
- Set impact tolerances for each important business service
- Test their ability to remain within their impact tolerances through severe disruption scenarios and conduct lessons learned exercises
- Develop internal and external communications plans to deal with disruptions and Create a self-assessment document

Comments on the FCA CP should be submitted on or before 3 April 2020.

CONDUCT REGULATION

FCA BOARD MINUTES: 23 AND 24 OCTOBER 2019

On 5 December, the FCA released the minutes of the FCA Board Meeting held on 23 and 24 October 2019. The Board discussed, among other issues, topics related to the update on UK's Withdrawal from the European Union, the ongoing negative cultural issues which were evident in elements of the wholesale insurance sector, issues related to access to cash specifically those relating to withdrawal of Barclays from the Post Office Banking Framework, and the circulation of the guidance that reminded FCA staff about the importance of political impartiality ahead of the planned election period.

QUARTERLY CONSULTATION NO 26 – CP19/33

On 6 December, the FCA published Consultation Paper (CP19/33) which proposes amendments to the FCA Handbook to clarify that the Financial Services Compensation Scheme (FSCS) can only consider one protected claim against either an appointed representative or a principal, up to the relevant limits set out in COMP 10.2.3R.

The Consultation Paper also proposes to clarify that FSCS claims can be made by an eligible claimant against a relevant person who has acted outside the scope of its permissions, including an appointed representative acting outside the scope of its agreement with the principal, in line with the relevant provisions in the Financial Services and Markets Act 2000.Comments should be submitted on or before 6 January 2020.

FCA EXTENDS THE SENIOR MANAGERS AND CERTIFICATION REGIME TO 47,000 FIRMS

On 9 December, the FCA extended the Senior Managers and Certification Regime (SM&CR) to around 47,000 firms across the UK financial services sector. The SM&CR already applied to the banking and insurance sectors and the FCA considers this extension as a key step to creating a culture across financial services where individuals take accountability for their own actions and competence.

By 9 December 2020, solo-regulated firms will need to ensure:

- all relevant staff are trained on the Conduct Rules and how they apply to their roles
- all staff in certified roles are fit and proper to perform that role and are issued with a certificate
- they submit data to us for the directory of key people working in financial services.

ELITE INSURANCE COMPANY LTD (‘ELITE’) HAS ENTERED INTO ADMINISTRATION

On 12 December, the FCA announced that Elite Insurance Company Ltd ("Elite"), an insurance firm authorised and regulated by the Gibraltar Financial Services Commission (GFSC), had entered into administration.

Elite ceased writing any new business in July 2017. The firm provided a range of insurance policies in the UK including Insurance-Backed warranties for white goods products, After the Event legal expenses insurance, latent defect construction insurance, alloy wheel warranty cover and Guaranteed Asset Protection (GAP) insurance.

The FCA noted that Elite policies do remain in force and are still valid, however advice should be sought from the brokers of effected policyholders on the alternative insurance covers available.

FCA HANDBOOK NOTICE NO.72

On 13 December, the FCA published a Handbook Notice describing the changes to the Handbook and other material made by the FCA Board on 21 November 2019 and 12 December 2019.

Chapter 2 of the Handbook Notice provides a summary of the changes.

Consultation feedback is published in Chapter 3, and FCA Board dates for 2019/20 are also listed within this Handbook Notice.

FCA ASKS FOR PROPOSALS ON HOW OPEN FINANCE COULD TRANSFORM FINANCIAL SERVICES

On 17 December, the FCA launched a Call for Input (CfI) on the opportunities presented by so-called 'open finance'. Open finance builds on the principles of open banking – the sharing of data which provides new ways for customers and businesses to make the most of their money. Open finance would extend those principles to a wider range of products.

By making it easier for consumers and businesses to compare price and product features and switch product or provider, open finance could be beneficial in the general insurance, cash savings and mortgage markets. It could help widen access to advice and support, boost efficiencies for businesses and access to credit, and spur innovation.

The CfI will launch a discussion on the opportunities and risks arising from open finance, what is needed to ensure it develops in the best interests of consumers, and what role the FCA should play. The FCA is seeking feedback to the CfI by 17 March 2020 and will publish a feedback statement in summer 2020.

ENFORCEMENT ACTION

FCA REGULATORY FINES ROUND-UP

FCA regulatory fines for 2019 now total £392.3m. The following fines and related enforcement actions have been announced in the past month:

Professional Personal Claims Limited	The FCA has fined Professional Personal Claims Limited (PPC) £70,000 for misleading consumers through its websites and printed materials. PPC was originally investigated and fined by the previous regulator for CMCs, the Claims Management Regulator (CMR), under the CMR's prior regulatory framework applicable before 1 April 2019. PPC's business focused on claims for redress for mis-sold PPI. On 5 December 2018, the CMR determined that PPC had breached the previous CMC conduct rules by using websites and marketing materials that were misleading and by submitting misleading material to financial firms in support of its clients' PPI redress claims. The CMR imposed a £70,000 fine for these failings. PPC appealed on 21 December 2018 to the First-tier Tribunal against the CMR's penalty notice. While the appeal was pending, the FCA took over regulation of CMCs from the CMR. The FCA therefore replaced the CMR as the respondent to PPC's pending appeal. On 16 September 2019, after reviewing the evidence put forward by the FCA, PPC withdrew its appeal, and the FCA therefore imposed the £70,000 fine on PPC for the failings identified in the CMR's penalty notice. PPC's websites and printed materials prominently used the logos of five major banks which was liable to mislead consumers into believing they were submitting redress claims for mis-sold payment protection insurance (PPI) directly to their banks, rather than engaging PPC as a CMC to pursue claims on their behalf in return for payment of a success fee. PPC also failed to present accurate, fully formed, detailed and specific complaints to banks. It had submitted Financial Ombudsman Service (FOS) questionnaires to banks on behalf of different consumers. The questionnaires in part contained identical factual allegations where evidence specific to each client should have been presented.
Hall and Hanley Limited	The First-tier Tribunal (the Tribunal) has upheld a fine of £91,000 imposed on Hall and Hanley Limited (H&H) by the Claims Management Regulator (CMR), the former regulator for claims management companies (CMCs). The hearing for the Tribunal was conducted by the FCA which has taken over the functions of the CMR. H&H is a CMC whose business focused on claims for mis-sold payment protection insurance (PPI). The £91,000 fine was initially imposed by the CMR under the previous regulatory regime for CMCs due to data breaches and unauthorised copying of client signatures. H&H appealed to the Tribunal against the fine. On 5 March 2019, the CMR found that H&H had breached rules requiring CMCs to take all reasonable steps to ensure that any referrals, leads or data purchased from third parties had been obtained in accordance with applicable laws. Marketing text messages concerning PPI claims were sent to consumers' mobile telephone numbers, without H&H

	having taken sufficient steps to check that affected consumers had consented to receiving such messages. In addition, when reviewing a sample of 16 of H&H's client files, the CMR found that in 8 of the files clients' signatures on claim documentation (including letters of authority) had been copied without authorisation. The CMR considered the unauthorised copying of clients' signatures, submitted by H&H to financial firms, to be a serious matter and considered H&H to have been negligent in failing to detect and prevent this conduct by one of its employees. The Tribunal upheld the CMR's decision in its entirety. In relation to data breaches, the Tribunal found that these were serious and followed from H&H not having taken previous compliance advice and warnings on board. It concluded that H&H failed to act with the required degree of competence and therefore acted negligently. Regarding the copied customer signatures, the Tribunal concluded that H&H acted negligently in failing to provide proper training and supervision to its employees, and that 'the underlying matter was so serious that a financial penalty is justified.'
Kevin Gorman	The FCA has fined Kevin Gorman, a former Managing Director at Braemar Shipping Services plc (Braemar), £45,000 for failure to notify personal trades. Mr Gorman carried out the trades in his capacity as a person discharging managerial responsibility (PDMR) at Braemar. Under the Market Abuse Regulations (MAR), persons who are PDMRs and those closely associated with them are required to notify the FCA and the issuer of every transaction conducted on their own account above a certain threshold within 3 business days. This includes transactions in the issuer's shares, debt instruments, derivatives or other linked financial instruments. Mr Gorman was found to have sold shares worth a total of £71,235.28 on 3 occasions between 24 August 2016 and 18 January 2017 without informing the FCA or Braemar within the required 3 business days. The FCA did not find that Mr Gorman traded whilst in possession of any confidential inside information. Senior managers notifying the FCA and issuers of their share transactions in a prompt manner is integral to transparency for market participants and maintaining confidence in the markets, as well as the FCA's effective supervision of the markets.

FCA SECURES CONFISCATION ORDER AGAINST ILLEGAL MONEY LENDER

On 11 December 2019, Southwark Crown Court made a confiscation order against Dharam Prakash Gopee in the sum of £5.1m. The effect of the order is to confiscate all his criminal proceeds as an illegal money lender. Mr Gopee was also ordered to pay almost £230,000 in compensation to consumers.

This followed the FCA's prosecution in which Mr Gopee was convicted of illegal money lending and sentenced to 3 and a half years in prison. Mr Gopee illegally loaned money to vulnerable consumers at high rates, securing the loans against their properties. He sought to take possession of the properties if the consumers failed to repay their loans. If Mr Gopee does not pay the confiscation and compensation orders on time, he is liable to spend a further 11 years in prison. Mr Gopee is also subject to a travel ban preventing him from leaving the UK until he has paid the orders.

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