INSURANCE REGULATORY EBULLETIN

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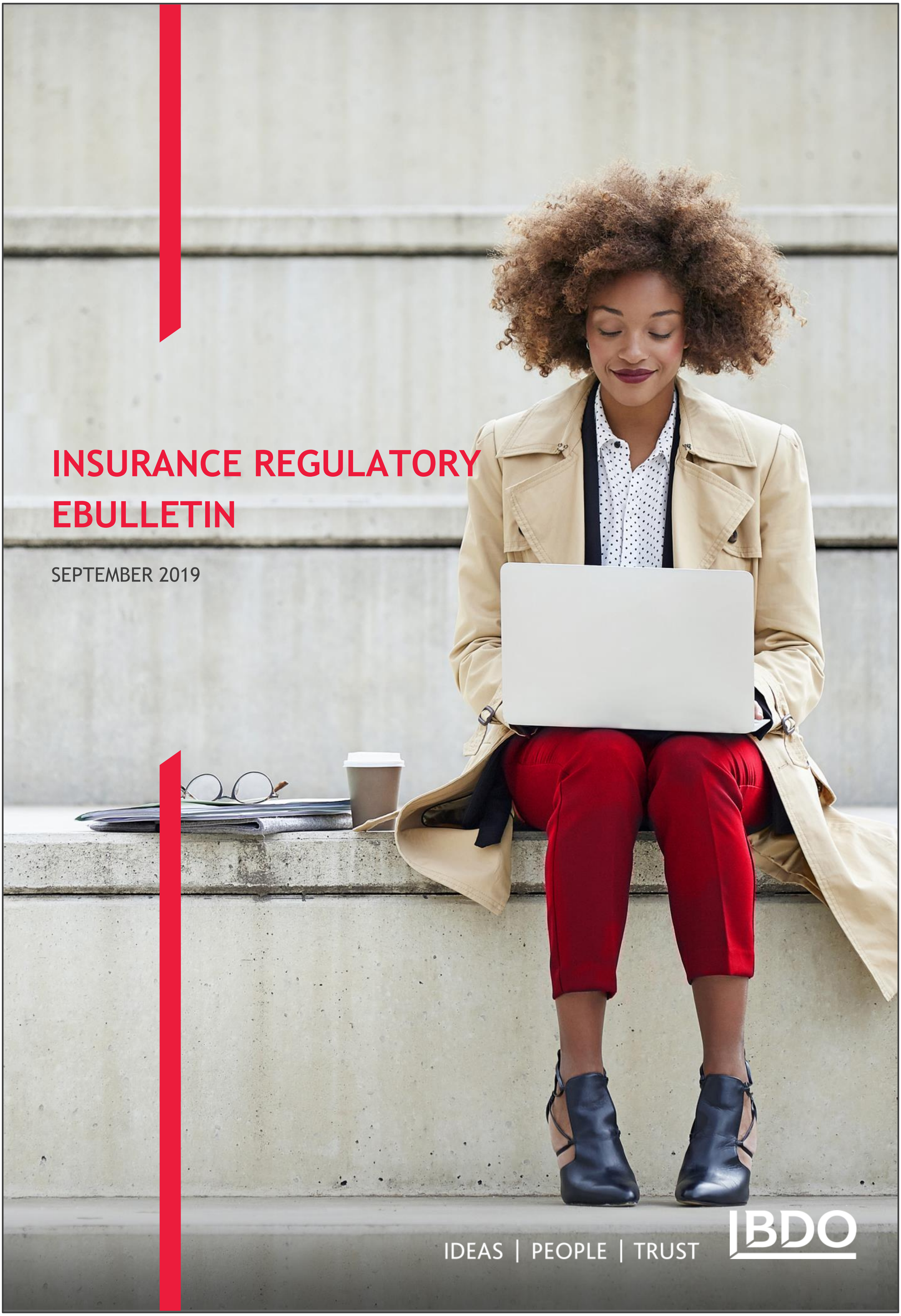

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WELCOME TO OUR INSURANCE REGULATORY EBULLETIN

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.

Another very quiet month on the regulatory front probably reflecting both the time of the year and the continuing uncertainty over Brexit. The FCA have been busy reminding firms of the need for appropriate Brexit planning and updating their SM&CR guidance. EIOPA has been considering cyber risk from both underwriting and operational risk perspectives and the PRA have issued a consultation on the Prudent Person Principle and finalised policy on liquidity risk management for insurers.

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

EU FINANCIAL REGULATORS HIGHLIGHT RISKS OF A NO-DEAL BREXIT AND SEARCH FOR YIELD

On 12 September, the European Banking Authority (EBA), European Insurance and Occupational Pensions Authority (EIOPA) and European Securities and Markets Authority (ESMA) (combined, the Joint Committee of the Supervisory Authorities (ESAs)) published the latest report on "Risks and Vulnerabilities in the EU Financial System".

The Report highlights the potential sources of instability as being:

- the uncertainties surrounding Brexit,
- persistently low interest rates,
- the transition to more sustainable economy and environmental, social and governance (ESG).
- The report is intended to promote supervisory vigilance and cooperation across all sectors and the ESAs call for policy actions related to contingency planning for Brexit, "Low-for-long" scenario risks, bank profitability and resilience in a more challenging environment, exploration of the risks in the leveraged lending market, and to continue the work on identifying exposures to climate related risks and facilitating access to sustainable assets for investors.

EIOPA ESTABLISHES CONSULTATIVE EXPERT GROUP ON DIGITAL ETHICS IN INSURANCE

On 17 September, EIOPA established its Consultative Expert Group on Digital Ethics in Insurance. The new Expert Group is a follow-up to EIOPA's recent thematic review on the use of Big Data Analytics (BDA) in motor and health insurance, EIOPA has established the Consultative Expert Group to assist the it in the development of digital responsibility principles in insurance.

The Consultative Expert Group may also act as a sounding board for EIOPA in other related policy initiatives in the area of InsurTech, for instance by supporting EIOPA in promoting a sound governance framework around the use of BDA tools such as Artificial Intelligence and Machine Learning.

The group will meet for the first time on Tuesday, 8 October.

CYBER RISK FOR INSURERS - CHALLENGES AND OPPORTUNITIES

On 17 September, EIOPA published its report on "Cyber Risk for Insurers – Challenges and Opportunities". The report discusses the factors that make insurers increasingly susceptible to cyber threats, such as the fast digital transformation, the increased use of cloud computing, and an increase in the frequency and sophistication of cyber-attacks.

The report identifies a need for a sound cyber resilience framework for insurers, consisting of clear, comprehensive and common requirements on the governance of cybersecurity as part of operational resilience measures.

However the report notes that not only are insurers susceptible to cyber threats directly themselves, but they also offer coverage for cyber risk through their underwriting activities. The report analysed cyber risk from both angles based on responses from 41 large (re)insurance groups across 12 European countries with the aim to further enhance the level of understanding of cyber risk for the European insurance sector.

Reviewing the EU cyber insurance market, the report finds that, although still small in size, the European cyber insurance industry is growing rapidly, with an increase of 72% in 2018 in terms of gross written premium for the insurers surveyed in the report, amounting to EUR 295 million in 2018 compared to EUR 172 million in 2017. However, non-affirmative cyber exposures (where cyber risk is neither explicitly included nor excluded within an insurance policy) remain a source of concern.

PRUDENTIAL REGULATION

INSURANCE SPECIAL PURPOSE VEHICLES: UPDATES TO AUTHORISATION AND SUPERVISION – CP19/19

On 3 September, the PRA published a Consultation Paper (CP19/19) on proposed updates to its approach and expectations in relation to the authorisation and supervision of Insurance Special Purpose Vehicles (ISPVs).

The proposals concern amendments to the ISPVs Part of the PRA Rulebook, including Supervisory Statement (SS) 8/17 'Authorisation and supervision of insurance special purpose vehicles', and the Multi-arrangement insurance special purpose vehicle New Risk Assumption Notification Form.

The proposals in the CP aim to provide further clarity and elaborate on certain additional aspects of the PRA's approach and expectations in relation to the authorisation and supervision of ISPVs. The Solvency II requirements in relation to ISPVs have not changed during this period but the PRA and applicants have gained experience of operating the regime in practice. The PRA considers that it would be helpful to update SS8/17 to reflect the experience gained over this period.

Responses to this consultation, including any other areas where further clarification on the PRA's approach to the authorisation or supervision of ISPVs would be useful, must be submitted by 3 December 2019.

SOLVENCY II: PRUDENT PERSON PRINCIPLE - CP22/19

On 18 September, the PRA published a Consultation Paper (CP22/19) on its proposed expectations for investment by firms pursuant to the Solvency II Prudent Person Principle (PPP) as specified in Chapters 2 to 5 of the Investments Part of the PRA Rulebook.

The draft Supervisory Statement sets out the PRA's proposed expectations for how firms manage investment risk in accordance with Rule 3.1 Conditions Governing Business and the PPP. These include expectations relating to:

- certain key elements of an insurer's investment governance and risk management framework
- management of asset concentration risk
- management of holdings of non-traded assets, including management of valuation risk
- assets backing technical provisions
- intra-group loans and participations.

The proposals are relevant to all UK Solvency II firms, mutuals, third-country branches, the Society of Lloyd's and its managing agents.

Comments should be submitted by 18 December 2019.

LIQUIDITY RISK MANAGEMENT FOR INSURERS – PS18/19 AND SS5/19

On 24 September, the PRA published a Policy Statement (PS18/19) which provides feedback to responses to its Consultation Paper (CP) 4/19 'Liquidity risk management for insurers'. The PS also contains the Supervisory Statement (SS5/19) 'Liquidity risk management for insurers'.

The PRA received thirteen responses to the CP, and after considering them, it has made some changes to the draft policy. The most significant amendments involve clarifying the PRA's expectations on the definition of risk limits within an insurer's liquidity risk appetite framework, the role of the board, and any risk committee of the board, in managing liquidity risk and the definition of the liquidity buffer. In addition, the function and characteristics of the liquidity buffer have been clarified.

The areas addressed in the SS include:

- the development and maintenance of proper policies, systems, controls and processes
- the identification of material liquidity risk drivers
- the design and undertaking of forward-looking scenario analysis and stress testing programmes
- considerations for the inclusion of highly liquid assets in the liquidity buffer
- the use of quantitative metrics and tools for measuring and monitoring liquidity risk drivers
- effective contingency planning.

The PS and SS are addressed to all UK Solvency II firms, including in respect of the Solvency II groups provisions, to the Society of Lloyd's ('the Society') and its managing agents, and to non-Directive insurers (collectively referred to as 'insurers').

INSURANCE RISK MANAGEMENT IN A CHANGING WORLD

On 24 September, Charlotte Gerken, PRA Director - Supervisory Risk Specialists, spoke at the Bank of America Merrill Lynch 24th Annual Financial CEO conference in London on the topic of 'Insurance risk management in a changing world'.

In the speech, she outlined some recent PRA policy that relates to the management of investment risk which includes the Consultation Paper on the Prudent Person Principle and a Supervisory Statement on liquidity risk management for insurers. She then looked ahead to emerging sources of risk such as cyber risk and cloud outsourcing and explained what the PRA is doing to address these and other emerging risks.

She concluded by noting that the principles of Solvency II remain as valid as the fundamentals of risk management and that in a uncertain world the management of, for example, concentration risk is more important than ever.

CONDUCT REGULATION

REGULATION ROUND UP

On 19 September, the FCA published its monthly Regulation round-up. The Hot Topics included Brexit preparations*, building cyber resilience and registering for Connect.

This edition included the following articles that are relevant to insurers or insurance intermediaries:

- Directory persons submission window which opens in September - Banks, building societies, credit unions and insurance companies must submit their data between 9 September and 9 March 2020 using Connect;
- Telling the FCA about competition investigations - some firms are not notifying the FCA immediately when a competition authority has started an investigation or imposed disciplinary measures or sanctions against them. Firms are required to notify the FCA in these circumstances.

* covered below

REGULATION ROUND-UP - BREXIT EDITION

On 12 September, the FCA published special edition of Regulation round-up which includes important information about preparing for Brexit.

The FCA urged all firms to consider the implications of a no-deal exit and finalise their preparations. Firms should have plans in place to address any risks for the firm and any impact it could have for customers.

The FCA drew particular attention to the fact that, in the event of a no-deal Brexit UK, firms doing business in the EEA through a passport will no longer be able to do so. Whether firms need regulatory permissions to continue to do business in an EEA country will depend on the activity they are carrying on, the local law and the approach of the local authorities in that jurisdiction. Firms should make themselves aware of any relevant transitional regimes, with deadlines or registration requirements attached to them, that have been put in place by relevant EEA Member States.

A list of dedicated Brexit websites hosted by financial regulators in EEA Member States that the FCA have been made aware of is available on the FCA website.

FCA STEPS UP EFFORTS TO ENSURE FIRMS ARE GETTING READY FOR A NO-DEAL BREXIT

On 11 September, the FCA issued a press release on stepping up efforts to ensure that firms are aware of what they need to do to prepare for a no-deal Brexit. The FCA will be running a series of digital adverts signposting to the FCA Brexit webpages, and has also set up a dedicated telephone line (0800 048 4255).

In addition, on 16 September the Financial Reporting Council (FRC) has written to Audit Committee Chairs and Finance Directors suggesting several of the most critical generic actions companies should consider prior to the UK's exit from the European Union.

Similarly, on 11 September the Information Commissioner's Office (ICO) has urged businesses to "prepare for all scenarios" as it published dedicated guidance to help small and medium sized organisations prepare for the possibility that the UK leaves the European Union with no deal. The guidance provides the same advice previously published on how to maintain data flows, but has been produced to be more relevant and accessible to smaller organisations.

The activities of the FCA, FRC and ICO are in support of the Government's efforts to raise the profile of the substantial material available to help companies ensure that they are best prepared for Brexit.

PREPARING FOR BREXIT IN FINANCIAL SERVICES: THE STATE OF PLAY - SPEECH

On 16 September, the FCA published a speech by FCA Chief Executive, Andrew Bailey, delivered at a Bloomberg event in London, regarding the current state of Brexit preparations at the FCA and in financial services.

Mr Bailey highlighted that the largest part of the overall Brexit preparation work concerns a no-deal scenario, because it would involve the largest change in short order. In this regard, he described the main developments in Brexit preparations. The FCA has worked closely with the Treasury and the Bank of England to ensure that EU financial services legislation is effectively on-shored by exit date. Presently, over 50 statutory instruments have been made to achieve this, with only a few outstanding.

Mr Bailey noted that the FCA will take on several functions concerning the UK which are presently performed by ESMA at the level of the EU, notably regulation of Credit Rating Agencies and Trade Repositories. Additionally, Mr Bailey welcomed steps already taken by UK and EU authorities to reduce the risks around continued access to UK and EU clearing services. In light of this, the UK government has legislated to allow UK businesses to use EU-based clearing houses for 3 years from the date of Brexit.

Regarding personal data, Mr Bailey added that the UK Government has legislated to allow the free flow of personal data from the UK to the EU in a no-deal scenario. However, without any action by EU authorities, EU rules would limit the flow of personal data from the EU to the UK. This, according to Mr Bailey, could restrict EU households and businesses from continuing contracts with, and accessing financial services from, UK financial service providers.

In concluding his speech, Mr Bailey reiterated the progress made on preparations in financial services. He further remarked that the FCA would continue to engage closely with its EU counterparts. In the FCA's view, the UK and the EU should be on a level playing field from day one due to having the same legislation and well established supervisory approaches.

IMPROVING THE SUITABILITY OF FINANCIAL ADVICE

On 19 September, Debbie Gupta, Director of Life Insurance and Financial Advice Supervision at the FCA, delivered a speech at the Money Marketing Interactive Conference 2019.

During the speech she noted that there are 4 broad areas of work the FCA are focusing on:

- improving standards,
- targeting firms that cause the most harm,
- supporting consumers and
- helping advisers.

She noted that the impact of poor quality advice cannot be easily undone or reversed and that advisers play an increasingly important role in the choices people make, and the impact of those choices on their quality of later life.

SENIOR MANAGERS AND CERTIFICATION REGIME: SOLO-REGULATED FIRMS

On 20 September, the FCA updated its website pages on the SM&CR for solo-regulated firms and has revised its SM&CR Guide for solo-regulated firms (updated July 2019) following the publication of the final rules and guidance.

The FCV have published two bite-size Inside FCA podcasts which will be useful for firms currently preparing for SM&CR. David Blunt, Head of Conduct Specialists at the FCA, explains the following topics:

- Certification and regulatory references: The purpose and scope, plus practical steps firms can take to prepare.
- Conduct rules: The five Conduct Rules will apply to everyone doing financial services work and the podcast explains the training requirements around them and offers practical tips for training staff.

The SM&CR will apply to almost all FSMA authorised firms from 9 December and affects almost every solo-regulated firm, from very small firms (including sole traders and limited permission consumer credit firms) to some of the largest global firms. It also applies to branches of non-UK firms with permission to carry out regulated activities in the UK.

ENFORCEMENT ACTION

FCA REGULATORY FINES ROUND-UP

FCA regulatory fines for 2019 now total £350.6m. No fines have been announced in the past month.

FOR MORE INFORMATION:

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