GIBRALTAR FINANCIAL SERVICES COMMISSION

Insurance Industry Event

Tuesday 21 March 2023

GIBRALTAR FINANCIAL SERVICES COMMISSION

Conduct of Business Supervision

GFSC Director of Authorisations & Conduct of Business

Amanda Eccleston

Introduction

- Starting position
- Current status and outcomes
- Future plans

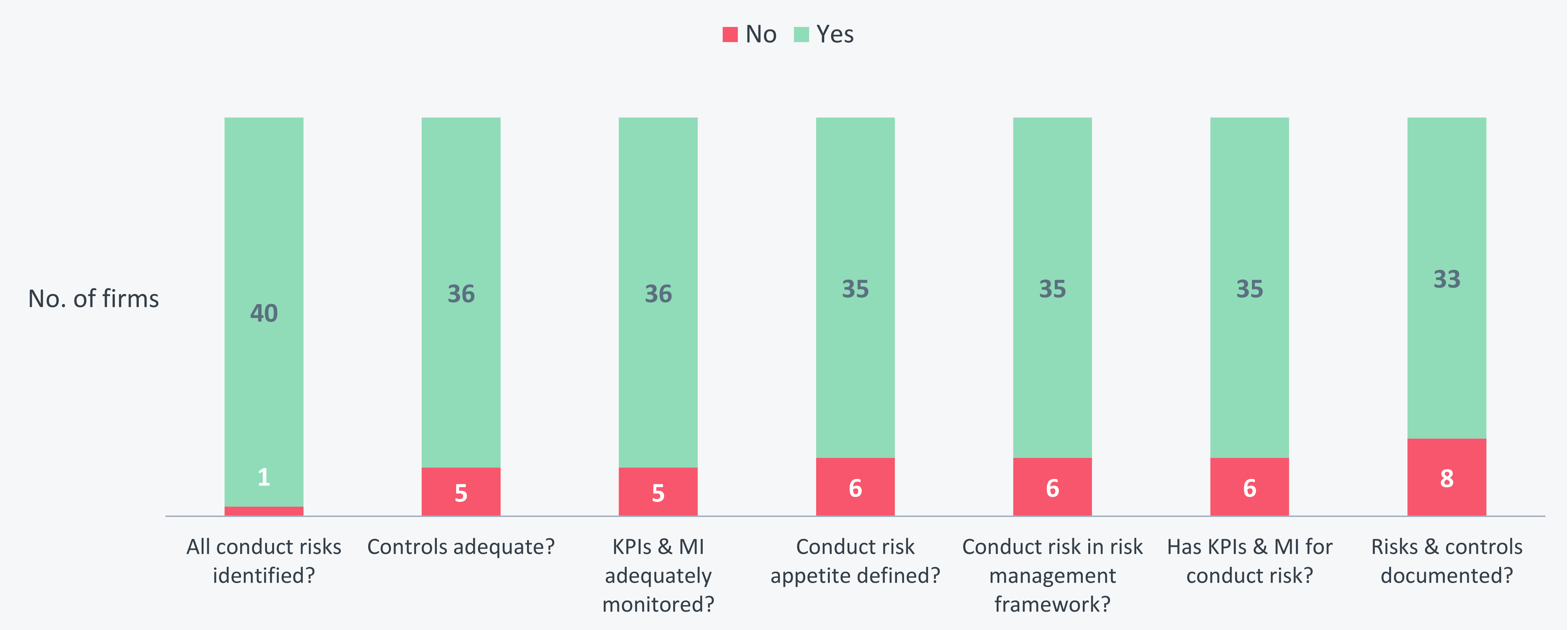
The starting position

- Risk based & reactive
- Limited data
- Lack of focus on **consumer outcomes**
- Strategic planning
- Recruitment

Current status

- Proactive plans
- Collaboration (industry, internal, external)
- Data collection and analysis
- Follow up work

Governance & Conduct Risk Framework



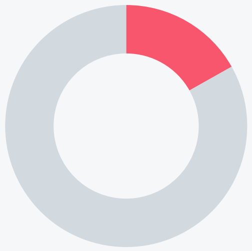
Observations - Conduct Risk Framework

- Difference in approach to managing consumer outcomes
- KRI’s and thresholds /appetites
- Evidence of monitoring
- Minutes lacking evidence of discussion

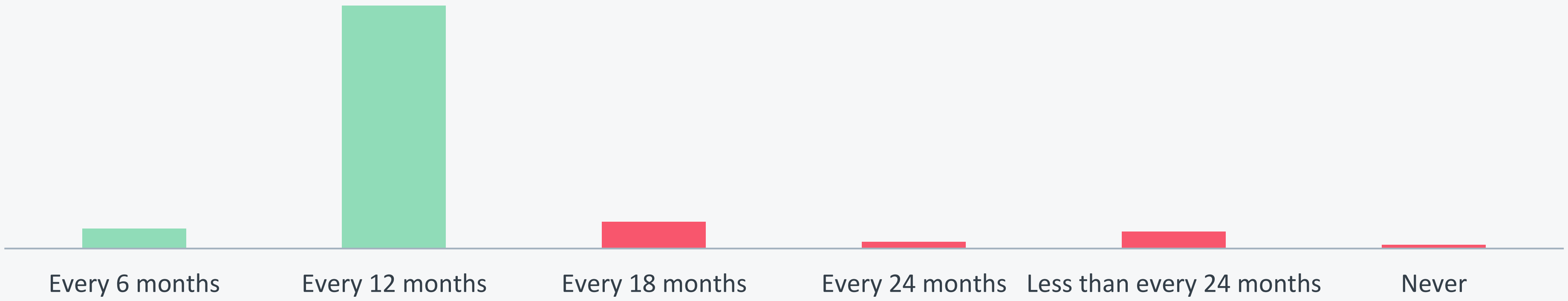
Product Governance

- A total of **22** new products were **manufactured.**
- A total of **63 significant product adaptations** were made.
- A total of **9 significant product adaptations** were made as result of **product reviews.**
- A total of **2** products were **withdrawn** as a result of product reviews.

17% of reviews were less often than yearly



Product reviews by frequency



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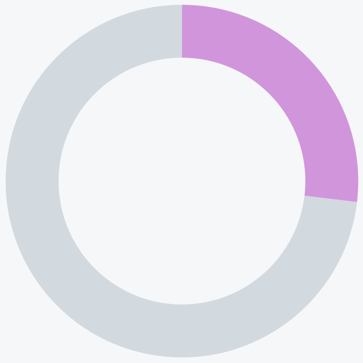
Observations – Product Governance

- Focus on financial performance
- Lack of evidence of discussions around consumers
- Frequency of product reviews
- Approval of new products

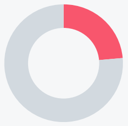
Observations - Customer documentation

73% of firms are responsible for customer documentation

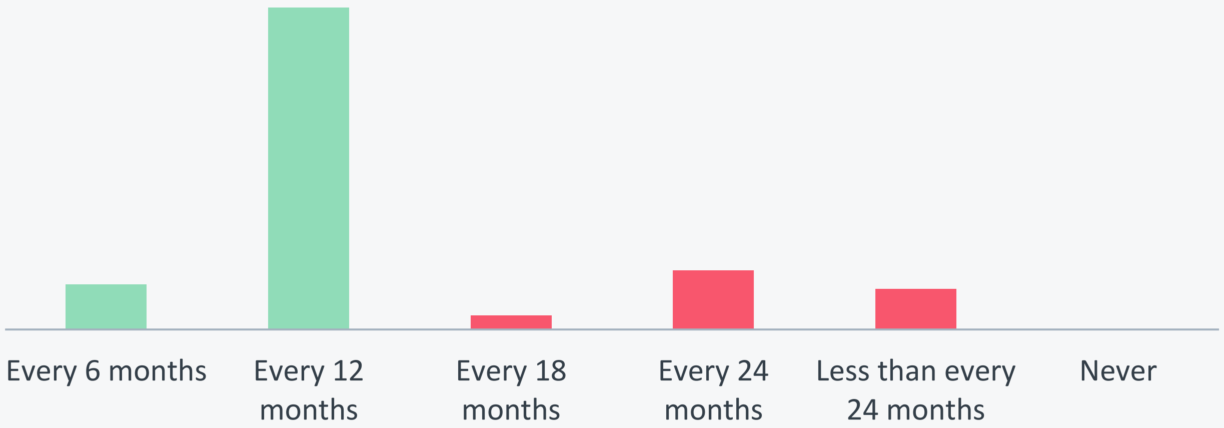


Of all firms that were responsible for customer documentation, **all except one** had policies & procedures for customer documentation

24% of reviews were less often than yearly



Customer documentation reviews by frequency



Observations - Complaints

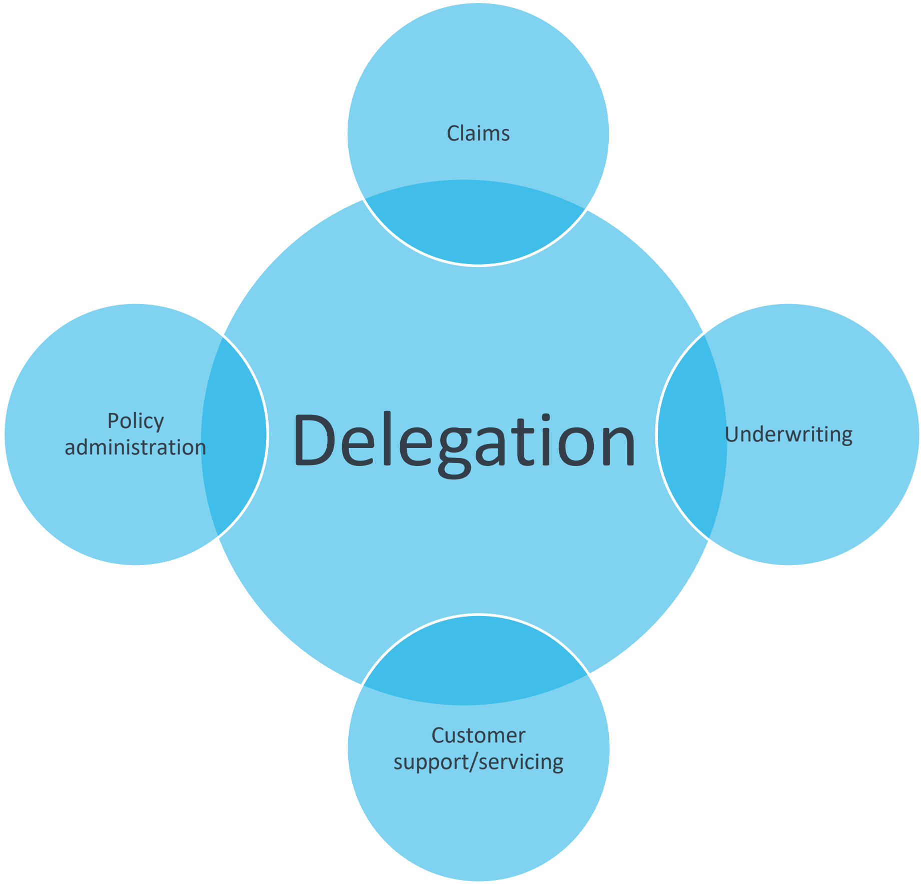
Intermediaries

Reason	No. complaints
Other	
Claim (declined due to lack of cover)	
Customer service (general)	
Claim (quality of repair or service)	
Policy (misleading wording)	
Renewal (unwanted)	
Claim (unsatisfactory settlement)	
Policy (details incorrect)	
Policy (pricing)	
Customer service (delay)	
Policy (lack of understanding)	
Renewal (timing)	
Claim (declined due to misrepresentation or non-disclosure)	
Renewal (pricing)	

Companies

Reason	No. complaints
Customer service (general)	
Other	
Claim (quality of repair or service)	
Policy (details incorrect)	
Policy (pricing)	
Customer service (delay)	
Claim (unsatisfactory settlement)	
Policy (misleading wording)	
Claim (declined due to lack of cover)	
Customer service (client account accessibility)	
Renewal (unwanted)	
Claim (declined due to misrepresentation or non-disclosure)	
Renewal (pricing)	
Policy (lack of understanding)	
Policy (mis-sold)	

Observations – Outsourcing



The future

- Consumer Duty – FCA
- Consumer Duty – Gibraltar
- Conduct return 2022
- KFH meetings
- Board/Committee minutes
- Risk assessments and actions (in line with Prudential team)
- Thematics and onsites
- Feedback

PWC's 2022 UK insurance sentiment index

- Price is a pull factor and service is push factor.
- Great experiences drive tangible growth.
- Customer 'experience' has the greatest impact on the three R's – Revenue, Retention and Reputation.

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Section 83A Financial Services Act 2019

GFSC Director of Prudential and Intensive Supervision

Joe Perdoni

Section 83A Consultation

- Reminder of the outcome S.83A is trying to achieve.
- Consultation update & next steps.
- Main feedback points:
  - Definition of material or significant
  - Pre-emptive & precautionary notifications
  - Timescales for GFSC response
  - Interplay with Notice of Requirements (NoRs)
  - Interplay with existing business planning/ORSA.

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Regulated Individuals

GFSC Director of Prudential and Intensive Supervision

Joe Perdoni

Regulated Individuals

GFSC letter in 2022 regarding Regulated Individuals (RIs).

Review identified a number of themes:

- Potential conflicts between role holders
- Whether firms are adequately meeting the substance requirements
- RIs with both governance and level 1 and 2 line of defence roles
- Waivers requested for Chief Operations Officer (COO).

Regulated Individuals

Following representations by industry, we are proposing:

- Allowing outsourcing of some of the Regulated Individual roles.
- Subject to:
  - Suitably addressing conflicts related to the role, remuneration & Incentives;
  - Contractual arrangements;
  - Meeting substance;
  - Proportionality.
- Exception regarding the Solvency II Compliance Function Holder:
  - Employee of the firm or outsourced to an insurance manager in Gibraltar.

Regulated Individuals

What the GFSC will be looking at when considering RI applications:

- Fitness and competence
- Overall skills mix
- Size of the in-house management team v Outsourcing
- Contractual arrangements
- Conflicts of interests in the role/remuneration arrangements.
- Segregation between:
  - Different lines of defence roles
  - The Executive Directors, Independent Non-Executive Directors (INEDs) and management functions.

Regulated Individuals

Reminder:

Please use the RI Application Form on the GFSC website and download it from there to ensure you are using the latest version.

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Update on prior year areas of focus

GFSC Head of Insurance
Monika Sookhee

Group Supervision

- Group supervision has been an area of priority.
- Key area of alignment under the GAR.
- Have an eye to the UK's implementation of Group Supervision following the issue of their supervisory statement earlier this year.
- We have been working with a number of firms to transition them to Solvency II insurance holding groups over the course of 2022 and 2023.
- This work stream is expected to continue into 2024 as we continue reviewing firm's group assessments.

Premium Debtors

- The objective of this work stream was to deliver a risk-based approach to the premium debtors review.
- We wrote to firms where we identified premium debtor days in excess of 25% of GwP.
- Where the appropriate SII risk charges were not being applied and this was seen as material, we have been working with firms on a transition plan to correctly apply the risk charges to their premium debtor balances.
- This work stream is expected to continue over 2023 as we work with firms through their transition plan and continue the review of the next group of firms in scope for the review.

Claims reviews

- The GFSC wrote to all third party writers to conduct a claims review, either as part of their internal audit process, or separately, as a one off, by an independent specialist claims handler over the course of Q2 and Q3 2022.

- A number of reports have been provided by firms to the GFSC, which considered the adequacy of the claims handling process in place, across the whole claims value chain, and consideration of the reserving philosophy and culture.

- Feedback from firms has been that the review has been very insightful, and of tremendous value. Firms have been able to identify areas of improvement which has saved them significant claims costs.

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Inflation

GFSC Head of Insurance
Monika Sookhee

Inflation

This has been a key area in our ORSA meetings and over the course of the year and continues to be an area of focus for 2023.

- GFSC communications to motor insurance firms in September 2022 requesting:
  - Inflation loadings
  - Average premiums and claims costs
  - Stress testing.
- PRA Dear Chief Actuary letter in October 2022.
- There is still uncertainty around inflation and how long it will persist.

Inflation

- Firms continue to navigate the uncertainties around inflation and build this into pricing models.
- Firms should work with their actuarial teams to:
  - Understand where and how inflation could manifest in current and future claims;
  - Understand the appropriateness of the reserving techniques being applied in the current environment;
  - Ensure there is an adequate feedback loop from claims to underwriting (pricing), reserving and capital modelling functions;
  - Ensure risk management systems continue to be effective;
  - Ensure that uncertainties relating to inflation are considered in the firm's risk appetite level and capital planning – challenge the status quo; and
  - Work with the actuaries (internal/external) to ensure that the reserving techniques remain appropriate - Board challenge/ training.

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Reinsurance
GFSC Director of Prudential Supervision
Kristian Menez

Reinsurance

- The GFSC expects firms to have reasonable levels of reinsurance.
- The core objective of the firm should be to generate reasonable underwriting profits.
- Reinsurance program should be complementary to Business Model and risk profile.
- We expect Boards to actively discuss the level of reinsurance as well as credit and concentration risk.
- Firms should consider the Prudent Person Principle in assessing this.
- The GFSC will be looking at how the overall level of firm and market reinsurance impact policyholder protection and systemic risk.

Reinsurance

- We have observed that high levels of reinsurance can lead to sub-optimal underwriting.
- This can occur where groups’ with intermediaries prioritise GwP volume and commissions over underwriting profits.
- This can also occur where groups’ set up subsidiaries and effectively reinsure the majority of the business.
- In addition to sub-optimal underwriting risk, the amount of credit/concentration risk can represent a large amount of the Balance Sheet.
- Sliding scales, sensitivity of Business Model, Standard Formula and Risk Transfer should be considered.

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Capital Planning

GFSC Director of Prudential Supervision

Kristian Menez

Optimism in capital planning and stress testing

- Firms should consider the whole of the economic and risk landscape when performing capital planning and stress testing.

- We continue to see business plans based on loss ratio which appear optimistic given current market conditions and historical performances.

- We also continue to observe firms' taking credit too early for the estimated effect that rate changes will have on the ULR before there is sufficient objective data to support this.

Optimism in capital planning and stress testing

- Additionally, the optimism seen is typically carried over to the level of assumed profitability when calculating their TPs and SCR.

- This can lead to inadequate reserving or underestimation in the assessment of capital requirements and is therefore a significant concern for the GFSC.

- The GFSC will closely scrutinise business and solvency forecasts and challenge firms where the future projected ULR differs significantly from the historic performance.

Optimism in capital planning and stress testing

- Where in particular there is interaction between a change of business plan and S83 we expect firms to have challenged themselves on the basis of the forecasts being presented and the downside risks to the business plan.

- An application for a material change in business plan where there is insufficient observable data to support change in key assumptions such as the estimated loss ratio from the historic performance is less likely to be approved.

What we expect in Capital Planning

- We will be looking for evidence of Board and Non-executive Director challenge.
- Consideration should be given to macro-economic and market factors and developments.
- There should be evidence of challenge around the major capital planning assumptions.
- We would generally expect to see use of latest IRR LR for capital modelling.
- We would not expect positive credit to be given for the re-underwriting of portfolios until this can be seen in data.

What we expect in Capital Planning

- More attention should be given to down-side risk and stress testing.
- The level of stress testing should be considered in the context of the variances in historic results of the firm.
- Consideration should be given as to the firms ability to underwrite stable ULRs over recent history and the variance against plan.
- An appropriate risk appetite SCR buffer should be set based on historic OF/SCR volatility.
- Firms should also consider sliding scale commission and standard formula appropriateness.

What we expect in Capital Planning

- We find it helpful where the plan sets out the KPI metrics that will be used to monitor actual vs expected results of underwriting.
- It is also helpful where firms provide clear, realistic and considered recovery actions where stress tests indicate that the SCR risk appetite buffer could be breached.

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Operational Resilience

GFSC Head of Policy
Julian Sacarello

Operational Resilience (OR)- background

- Regulators' concerns that firms were not sufficiently prepared to deal with fallout from significant disruptions like tech outages, cybersecurity threats, data loss, pandemics.
- OR regime is concerned with the ability of firms and the financial sector as a whole to prevent, adapt and respond to, recover and learn from operational disruption.
- OR based on the assumption that disruptions will prevent firms from operating as usual and see them unable to provide their services for a period of time.
- Rules require firms to set and meet clear standards for the services they provide and test their ability to meet those standards. Requirement to review their approaches and make improvements where necessary.
- **Desired outcome is that firms can remain within their Impact Tolerance for their Important Business Services by responding effectively to disruption and continuing to deliver such services.**

GAR- UK alignment

- Gibraltar's financial services legislation and our supervisory practices need to be aligned with the UK in areas of mutual market access.
- This is enhanced by the Gibraltar Authorisation Regime (GAR) which will commence in the next couple of years.
- Prior to the GAR coming into force the UK will conduct sectoral assessments to ensure there is sufficient alignment (both in terms law and practice).
- Operational Resilience needs to be implemented as soon as possible.

Key features of OR- Important Business Services and Impact Tolerance

- OR is based around the requirement for firms to identify what their **Important Business Services** are, and to set an **Impact Tolerance** for each of these.
- Important Business Services are services a firm provides to a client which, if disrupted, could;

1. cause an intolerable level of harm to one or more of its clients; **or**

2. Pose a risk to the firm's safety and soundness, an appropriate degree of protection for the firm's policyholders, the orderly operation of the financial markets **<u>or</u>** the soundness stability or resilience of the financial system.

Key features- Impact Tolerance

- The maximum tolerable level of disruption for an Important Business Service.
- Tolerance must be set at the point at which disruption to a firm's Important Business Services **would** meet the criteria set out in the previous slide.
- The Impact Tolerance must be measured by a length of time for which the disruption can be tolerated, and any other relevant metrics .
- Firms must ensure they can remain within impact tolerance for each Important Business Service in the event of a severe but plausible disruption to their operations.
- **Mapping** and testing the delivery of important business services will enable firms to determine whether and how they can remain within impact tolerances.

Key features- Mapping and scenario testing

- **Mapping**- Firms required to identify and document the necessary people, processes, technology, facilities, and information (the ‘resources’) required to deliver each of their Important Business Service.
- **Scenario testing-** Firms required to regularly test their ability to remain within impact tolerances for their Important Business Services in severe but plausible disruption scenarios.
- Firms should document findings and use these to inform their OR measures, which should ensure they are able to remain within impact tolerances.

Gibraltar approach to the legislation

- Gibraltar regulations
- Will incorporate the content of the FCA and PRA rules as well as some of the additional FCA guidance content
- Important for alignment- sufficient alignment required
- 1 year implementation period from the day legislation commences (April 2023 legislation published)
- Firms expected to identify Important Business Services, set IT and conduct mapping exercises
- 3 years from the legislation commencing, firms demonstrate they can remain within impact tolerances (**April 2026**)

Questions

Comments