

# Areas of supervisory focus for insurance 2022



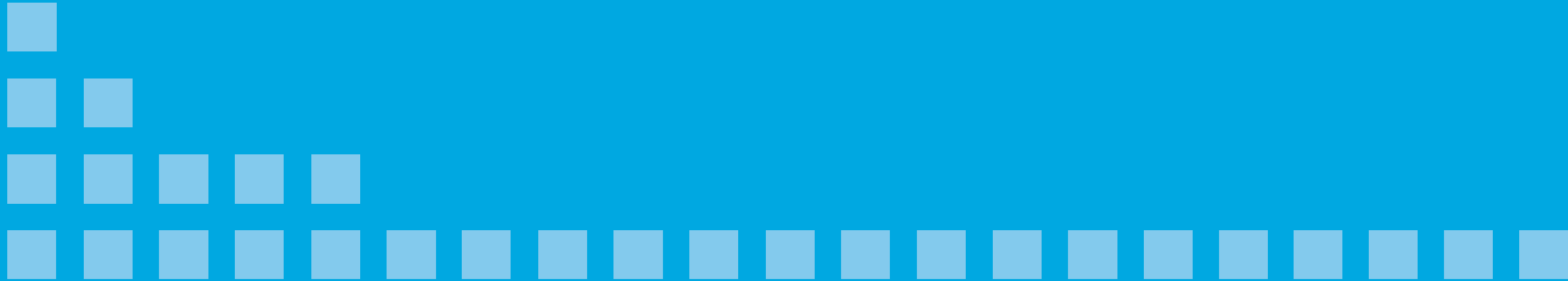
# Agenda

1. Welcome and introduction
2. Address by Minister for Digital and Financial Services
3. Group supervision
4. Premium debtors
5. Substance and regulated individuals
6. Claims reviews
7. Q&A

# Questions

- Please send any questions on the chat function.
- We will be monitoring questions throughout the presentation and will answer these are the end.

# Group Supervision



# Group Supervision

Group Supervision is important for a number of reasons:

- It safeguards insurance companies to the extent that the overall group risks are monitored and supervised.
- It helps to reduce the conflicts of interests that arise between the distribution and insurance business units of the group.
- It focuses attention on group governance.
- It focuses attention on the group solvency capital requirements.
- It aims to reduce the risks arising from debt finance and senior debt charges within the insurance holding group and hence the risk to policyholder premiums and claims payments.

# Group Supervision

When reviewing insurance groups, we have considered the following:

- Whether supervision should be at the ultimate holding company level.
- Whether there is equivalence at the ultimate holding company level.
- Taking into account the underwriting and distribution sides as well as any service companies.
- Both capital and operational risk mitigation as well as independence of governance of the insurer and any related service companies.

# Group Supervision

When reviewing whether an insurance group is mixed activity or an insurance group, we have been considering:

- Metrics - as published in existing Guidance Note 13.
- Group Risks and Group Contagion.
- Possible changes in classification.
- The independence of decision making and operations of the insurer.
- If there is, or should be a sub-IHG within any Mixed Activity Group.

We also note the publication of the PRA consultation CP17/21 - Solvency II: Definition of an insurance holding company and will consider whether further consultation and guidance would be helpful in this area.

## Proposed Metrics going forward

- 50% of gross assets or net assets
  - 50% of gross or net revenue
  - Contribution to the consolidated group SCR
  - 50% of assets and revenues net of intra group transactions
- Use whichever is most prudent.

Firms should consider nature of services provided by brokers and MGAs and level of outsourcing and delegation

# Ancillary services

## Solvency II Delegated Regulation – Article 1 Definitions

‘Ancillary services undertaking’ means a non-regulated undertaking the principal activity of which consists of

- owning or managing property,
- managing data-processing services,
- health and care services
- or any other similar activity which is ancillary to the principal activity of one or more insurance or reinsurance undertakings.

## Definition of ancillary in English language

Providing necessary support to the main work or activities of an organisation (Oxford learners dictionary)

Providing support or help (Cambridge dictionary)



# Summary on group supervision

- The objective of group supervision is to safeguard insurance companies and their consumers to the extent that group risks are monitored and supervised.
- When considering insurance groups, we consider whether supervision should be applied at the ultimate holding company level or Gibraltar/UK level.
- Holding Company assessments are based on the metrics set out in Guidance note 13. Where the insurer and its service entity have strong interdependencies, we will consider whether an insurance sub-group should be formed in a wider mixed activity group.
- Where debt exists in an insurance group the risk to policyholder claims and premiums are the same, irrespective of whether the group is an insurance holding company or a mixed activity insurance group.
- The GFSC will be looking to the PRA consultation in this area and consider whether similar guidance will be issued.

# Next steps on group supervision

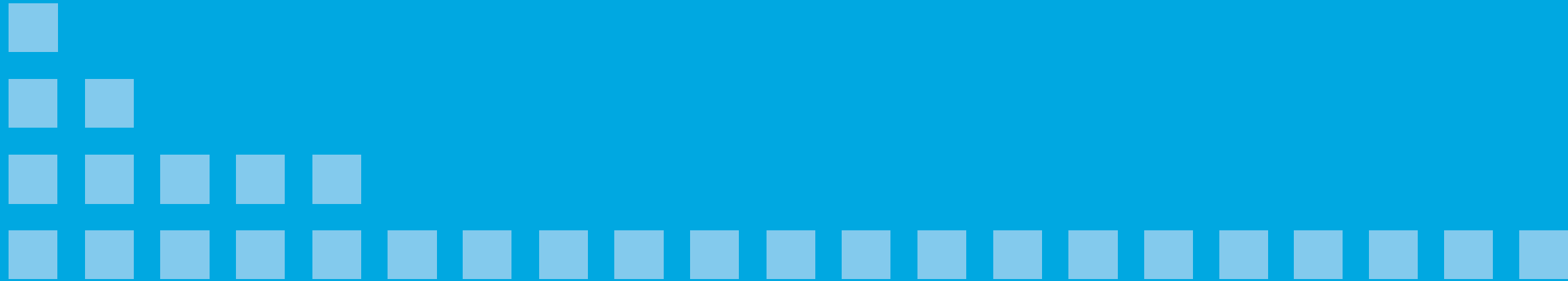
## What firms should do

- Firms should periodically assess the status of any wider group which they belong to
- Firms should consider any forward looking plans against any potential impact on the group status
- Where the group status could change, firms should have a transition plan in place to ensure that they would be able to comply with the group supervision requirements post change
- Firms should consider the presentation today and any changes which could arise from the PRA CP

## What the GFSC is proposing to do

- Where this is a supervisory focus area for firms, this will be communicated in the annual supervisory letter where relevant
- The GFSC will engage with firms to assess the group status and transition to group supervision where relevant
- The GFSC will be matching to a large degree any guidance note issued by the PRA

# Premium Debtors



# Premium debtors

- In 2021 we conducted a series of focused reviews which considered premium and other debtor exposures and agreements with intermediaries.
- We considered the nature of the arrangements companies had in place
- Our findings highlighted a wide discrepancy in the market as to how these were being treated
- Some firms are not holding capital or incorporating a risk charge for exposures to insurance brokers and MGAs
- Historic failures in Gibraltar have also highlighted the challenges in recovering funds from brokers in stressed scenarios
- This is therefore a priority area for the FSC in 2022

# Solvency II treatment of insurance contracts

## Legal framework

- High level regulations set out in the Financial Services (Insurance Companies) Regulations 2020
- Further detailed regulations set out in the Solvency II Delegated Regulation

## Guidance

- Guidelines on the valuation of technical provisions

# Recognition and derecognition

## Solvency II Delegated Regulation

**Article 17** – Covers the recognition and derecognition of an insurance contract and obligation.

Undertakings shall recognise an insurance or reinsurance obligation at the date:

- the undertaking becomes a party to the contract that gives rise to the obligation or the date the insurance or reinsurance cover begins, whichever date occurs earlier.
- shall only recognise the obligations within the boundary of the contract.
- shall derecognise an insurance or reinsurance obligation only when it is extinguished, discharged, cancelled or expires.

# Contract boundaries

## Solvency II Delegated Regulation

Article 18 – covers the rules related to contract boundaries.

- Firms must consider the insurance contract entered with policyholders.

# Technical provisions and debtors

## Solvency II Delegated Regulation and Guidelines

**Article 28** – covers the rules related to cash flows included within technical provisions however the Guidelines on the valuation of the technical provisions issued alongside Solvency II set out the following in guideline 68:

1.122. Insurance and reinsurance undertakings should establish the future premium cash-flows contained within the contract boundaries at the valuation date and include within the calculation of its best estimate liabilities those future premium cash-flows which fall due after the valuation date.

1.123. Insurance and reinsurance undertakings should treat premiums which are due for payment by the valuation date as a premium receivable on its balance sheet until the cash is received.



# Premium debtors

## EIOPA Q&A with regards to Premium Receivables

Q: Can you please clarify the treatment of premium receivables, which cover exposure periods, which start prior to the valuation date and finish after the valuation date, and which are considered due under the terms of the policy agreement and have a credit arrangement that goes beyond the valuation date?

A: Premiums which have fallen due and have not yet been received (regardless of whether a credit period exists or not) should be considered as assets on the Balance Sheet (i.e. not TP).”

# Counterparty default

Financial Services (Insurance Companies) Regulations 2020  
(the “Regulations”)

The Regulations set out the following in Regulation 95:

(6) The counterparty default risk module–

- must cover ..... receivables from intermediaries, as well as any other credit exposures which are not covered in the spread risk sub-module;
- for each counterparty, must take account of the overall counterparty risk exposure of the undertaking to that counterparty, irrespective of the legal form of its contractual obligations to that undertaking.

Article 202 Solvency II  
Delegated Regulation

- Amounts due < 3 months  
– 15% risk charge
- Amounts due > 3 months  
– 90% risk charge

# Lapse risk module

## Article 118 Solvency II Delegated Regulation

### Non-life lapse risk sub-module

- The capital requirement is 40 % of current or future insurance policies for which discontinuance would result in an increase of technical provisions without the risk margin
- The undertaking shall base the calculation on the type of discontinuance which most negatively affects the basic own funds of the undertaking on a per policy basis
- The 'discontinuance' of an insurance policy means surrender, lapse without value, making a contract paid-up, automatic non-forfeiture provisions or exercising other discontinuity options or not exercising continuity options

# Standard formula appropriateness

Financial Services (Insurance Companies) Regulations 2020 (the “Regulations”)

## **Standard formula appropriateness**

The company should also consider standard formula appropriateness as set out in Regulation 46(1)(c) of the Regulations. That assessment must include:

- the overall solvency needs taking into account the specific risk profile, approved risk tolerance limits and the business strategy of the undertaking
- the compliance, on a continuous basis, with the capital requirements and technical provisions
- the significance with which the risk profile of the undertaking deviates from the assumptions underlying the Solvency Capital Requirement

# Summary on premium debtors

## Overview

- Companies should consider insurance contracts and insurance obligations within contract boundaries with policyholders per Articles 17 and 18 of the SII Delegated Regulation.
- Amounts due for payment in relation to periods of cover prior to the valuation date should generally be included as amounts receivable and included in the counterparty default module.
- The counterparty default should cover receivables from intermediaries, as well as any other credit exposures and must take account of the overall counterparty risk exposure of the undertaking to that counterparty, irrespective of the legal form of its contractual obligations to that undertaking.

# Summary on premium debtors

## Overview

- When considering the lapse stress within technical provisions the requirement is to consider the most adverse discontinuance on the own funds of the firm.
- The 'discontinuance' of an insurance policy means surrender, lapse without value, making a contract paid-up, automatic non-forfeiture provisions or exercising other discontinuity options or not exercising continuity options.
- Companies should consider standard formula appropriateness and assess whether the risk profile of the undertaking and relevant arrangements deviates from the assumptions underlying the Solvency Capital Requirement. The FSC would generally consider this to apply where contracts are entered into with connected parties with credit terms > 60 days.

# Next steps on premium debtors

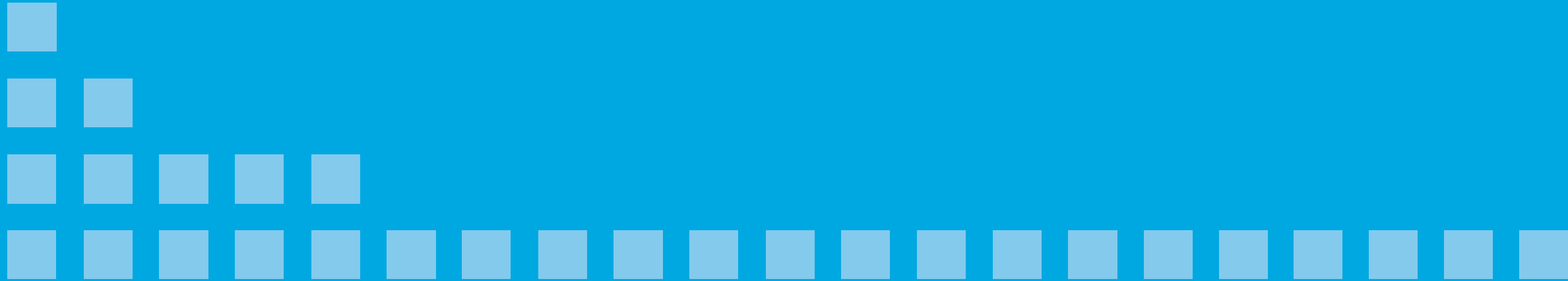
## What firms should do

- Firms should consider the material and clarifications provided today
- Firms should assess whether they are treating insurance contracts in line with the material set out today
- Firms should prepare an assessment and any necessary transition plan needed to be ready for when the GFSC contact them

## What the GFSC is proposing to do

- The GFSC will be issuing a Dear CEO letter on this topic for firms to consider
- The GFSC will be writing to firms to request an assessment of how firms treat insurance contracts and obligations within technical provisions, the counterparty default module and the lapse risk module
- The GFSC will expect a transition plan for any changes needed to the treatment and any consequential impact on the SCR cover of the firm

# Regulated Individuals & Substance





# Regulated individuals

## Regulated Individuals Regime

The regulated individuals regime came into force in 2020 as part of the LRP. Schedule 14 & 15 of the Financial Services Act sets out the types of regulated functions, those that are mandatory and those that can be waived. These roles are:

FSA 2019		Role
<b>SCHEDULE 14</b>	<i>All RI firms</i>	Head of Compliance
		Executive Director
		Branch manager (if firm has branches in the EEA)
<b>SCHEDULE 15</b>	<i>Insurance and reinsurance undertakings</i>	Head of Actuarial Function
		Head of Internal Audit
		Head of Risk Management
		Head of Finance
		Chair
<b>SCHEDULE 15</b>		Chief Executive/Managing Director
		Chair of the Risk committee
		Chair of the Audit committee
		Head of Finance
		Chief Operating Officer
		Head of Underwriting
<b>SCHEDULE 15</b>		Head of Claims

### Proposed approach for waiver requests

The firm should write to the GFSC requesting a waiver for a Schedule 15 role. The waiver request must explain the rationale for why this role is not relevant or needed for the insurance company.

# Regulated individuals – conflicts of interest

- Where certain roles are filled by individuals who also perform functions for the insurance intermediary or key outsourced service provider, the GFSC would like to see firms consider whether any conflicts would arise from this
- Depending on the size and complexity of the firm, there could be more than one role undertaken by one individual. Conflicts of interest should be considered in these circumstances
- Conflicts could also apply at individual level depending on remuneration and incentives
- Conflicts can likely be improved through having a good balance of Executive Directors to Independent Non Executive Directors
- Head of Underwriting and Head of Claims - Conflicts are likely to exist between these two roles

The GFSC is considering whether further consultation and guidance would be helpful in this area

# Substance

## Substance/Head office

An applicant or insurance company must meet the threshold condition for location of its offices set out in paragraph 1 of Schedule 12 to the FSA 2019.

We expect Gibraltar firms to be controlled by their Boards and senior management from Gibraltar. We therefore expect that firms have a substantive presence ***with the majority of their senior role holders (i.e. individuals carrying out regulated functions under Part 8 of the FSA 2019) based in Gibraltar the majority of the time.***

# Summary on Regulated Individuals

- All schedule 14 & 15 roles are required to be filled, unless a waiver has been granted by the GFSC.
- Should there be any roles that still need to be filled, firms should send a transition plan to the GFSC.
- Any appointments will need to follow the standard RI process.
- Firms should consider conflicts of interest arising when proposing appointments for role holders.
- Firms must be controlled by their Boards from Gibraltar – this means that we expect to see that majority of the senior role holders based in Gibraltar for the majority of the time.

# Next steps on regulated individuals

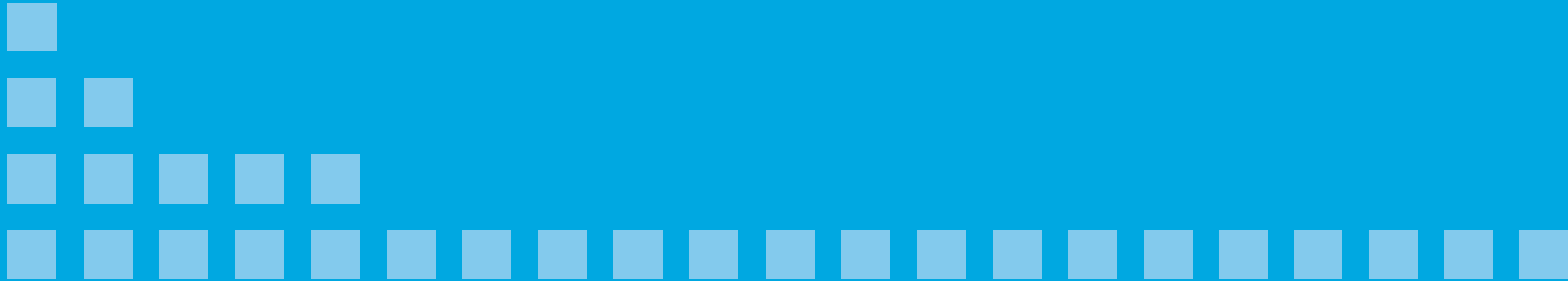
## What firms should do

- Firms should consider whether they have in place (or have waivers for) the roles set out in schedule 14 & 15 of the FSA.
- Firms should assess whether the majority of these roles are based in Gibraltar
- Firms should write to us with the names and location of the role holders. Should one or more of the roles not be filled, the firm should write to us with a plan (including timelines) on when these positions will be filled (or requesting a waiver with the rationale for why this role is not needed).
- Any applications for RIs will be subject to the usual RI application process.


## What the GFSC is proposing to do

- The GFSC will be writing to firms to request a list of all schedule 14 & 15 roleholders and their location.
- The GFSC will expect a transition plan for any roles that are not filled (for which a waiver does not exist).
- Any applications for RIs will be subject to the usual RI application process.

# Claims Reviews



# Claims Reviews

- Importance of high quality claims handling & claims reserve setting
- Poor claims data in  poor claims reserves out
- Additional risks re related party claims handling/broker/MGA
- Importance of regular reviews of claims functions
- Expect all firms to conduct a review of claims function as part of the internal audit cycle
  - By independent specialist firm
  - Claims notification, evaluation and verification, claims reserving

# Claims Reviews (Cont....)

## – Review of claims files:

- FNoL, Timeliness of reserve updates
- Claims leakage, original claim estimate v final settled amount
- Static claims, Nil reserve claims, reopening of closed claims
- Backlogs
- Claims inflation
- Management override

## Next Steps on Claims Review

- Firms should ensure that adequate controls and process exist over claims and that these are subject to an independent review on a periodic basis
- Certain firms will be contacted to conduct a review in Q2 2022



Q&A