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# Insurance regulation newsletter
# **Issue 3 – October 2022**

**Inflationary pressure was the dominant discussion topic across all facets of society during Q3 2022 and insurance was certainly no exception to this. How insurers, and indeed regulators, react to this period of volatility is expected to remain a key area of focus for the duration of 2022 and beyond. But the current economic situation should not distract from the increasing regulatory expectations around climate, intra-group and outsourcing governance arrangements, and conduct risk. The Mazars Insurance Regulation Newsletter provides a flavour of the latest developments that insurers should be aware of.**

Financial and operational resilience has been a hot regulatory topic of late – the Central Bank of Ireland's Pre-Emptive Recovery Plan requirements are just one recent example of this. On the back of the requirement for all insurers to put documented plans in place earlier this year, Mazars conducted an industry survey to gauge the challenges and obstacles faced in complying with the new regulations. We are delighted to now share the results of the survey which are both intriguing and informative. This is discussed further in Section 1 of the newsletter.

Climate and sustainability matters rightfully maintained its place as a key focus of both EIOPA and the CBI last quarter. The CBI's Consultation Paper (CP151) gives insurers plenty of food for thought on their risks and obligations with regards to climate risk. Meanwhile, EIOPA have been extremely active publishing guidance on climate risk in the ORSA, guidance on sustainability preferences under the Insurance Distribution Directive ("IDD"), and have been actively pushing for more transparent disclosures under the Sustainable Finance Disclosure Regulations ("SFDR").

Elsewhere, on the domestic front, the CBI have shown no reservation in displaying the full extent of their enforcement powers. A record fine in excess of €100m was imposed upon one of the domestic banks while a smaller, but a first of its kind fine was imposed on a financial institution supervised outside of Ireland that passports to an Irish branch. This more visible enforcement activity comes at a time in which the Senior Executive Accountability Regime ("SEAR") bill is progressing through the legislative stages.

The CBI's recent focus areas have also included intragroup risk, outsourcing governance and a public consultation on the Consumer Protection Code ("CPC").

Similar regulatory themes are been echoed from Europe. EIOPA's recently updated programme of work places emphasis on digital resilience, IORP II implementation, climate risk, cross-border risk and inflation. Quite a number of Consultation Papers and Supervisory Statements were published spanning third-country governance, differential pricing, outsourcing, cyber, and systemic events.

Finally, from a general insurance perspective, many domestic insurers are welcoming recent developments regarding personal injuries claims treatment. Publication of recent legislative bills, high court judgement developments and preliminary claims statistics all point towards eventual reductions in insurance costs for end customers.

As always, the Mazars in Ireland insurance team is on hand to guide our clients through the changes and challenges ahead.

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# Pre-emptive recovery planning
## Mazars industry survey results

**Following the Recovery Plan Requirements for Insurers Regulations 2021, insurance and reinsurance undertakings were required to have documented Pre-Emptive Recovery Plans in place from 31 March 2022.**

On the back of this, Mazars in Ireland observed high demand from its insurance clients and contacts for peer benchmarking outlining how (re)insurers have faired in their initial recovery planning journey. So, over the summer of 2022 we conducted an extensive industry survey and we are now pleased to share insights.

### Recovery Plan Report Style & Content

Pre-Emptive Recovery Plan documents tend to be quite substantial documents, with 55% of our survey participants stating that their report was at least 60 pages in length. Life company participants tended to have longer reports than non-life entities.

The sections of the recovery plan which proved to be most challenging were Scenario Analysis (41%), Recovery Options (27%) and Information on Preparatory Measures (14%).

### Governance

77% of companies said their CRO / Risk function owns the Recovery Plan at executive level. 73% of life companies said the Recovery Plan is highly integrated into existing systems of governance and risk management frameworks. Most non-life entities consider that theirs were somewhat integrated but more work is needed in this area.

### Recovery Indicators

Insurers with higher PRISM ratings tended to have more recovery indicators in place than lower rated entities. The most common volume of indicators is 4 – 10. This range was typical across all PRISM ratings and segments of the market. 32% use either 2 or 3 indicators, and these tended to be mostly Low and Medium-Low rated entities. Three life companies used over 10 indicators. The majority of firms (77%) plan to update / recalculate / monitor recovery indicators quarterly.

The setting of Recovery Indicator Thresholds is an area that currently relies quite heavily on judgement, especially in the case of non-life insurers. Life companies seem to be further along the path to using sophisticated scientific approaches.

### Integration with ORSA

Most companies said that the ORSA was somewhat connected with the recovery plans (68%), with life company responses being more skewed towards higher level of integration, while non-life responses were more skewed towards limited connections between the two.

The majority of companies (55%) said their ORSA only models adverse outcomes and does not model recovery options. However, all High rated insurers said their ORSA models several recovery options.

### Scenario Analysis

59% of insurers considered four or less scenarios in their scenario analysis. Just 9% of insurers use more than 10 scenarios. Higher rated firms showed a slight trend of using more scenarios than lower rated insurers. The majority of insurers (64%) said a cross-departmental working group was in charge of developing and assessing the scenarios for the Recovery Plan. The trend was similar across different insurer type and PRISM ratings.

Please click on this link to go to the detailed survey results.

## Spotlight on Climate

**Climate expectations and climate regulations remain at the forefront of activity at both Irish and European level. There is an increasing volume of guidelines and requirements which (re)insurers are expected to remain abreast of.**

### Consultation Paper 151 – Guidance for (Re)insurance Undertakings on Climate Change Risk

The CBI launched a consultation, CP151, on climate risk guidance for the insurance sector on 3 August. The proposed Guidance aims to clarify the Central Bank's expectations on how (re)insurers address climate change risks in their business and to assist them in developing their governance and risk management frameworks to do so.

The paper introduces several overarching principles including the need for an iterative approach, an expectation to consider climate as an ongoing rather than emerging risk, and the concept of 'Double Materiality' which recognises insurers' unique profile with regards to climate risk. Insurers' own activities are of course exposed to the climate (outside-in risk). But also, the activities of insurers, and the activities they choose to underwrite, can pose a risk to the climate (inside-out risk). There have also been some much sought after clarifications on Time Horizon definitions (which in some instances are much longer than insurers are accustomed to considering).

Aside from the key principles, there is also very useful guidance on Governance, Materiality Assessments, the ORSA, Business Strategy, Risk Appetite and Risk Management. Expectations around Reserving, Capital, Underwriting, Pricing and Investments are also considered.

The CBI has also created a corresponding infographic to provide a visual overview of the approach to the assessment and ongoing management of a (re)insurer's exposure to climate change risk.

The consultation process runs until 26 October.

### EIOPA publishes application guidance on how to reflect climate change in the ORSA

In August, EIOPA published the final version of the application guidance following a prior public consultation.

According to EIOPA:

*"The application guidance provides a detailed and practical basis on how to implement sustainable finance ambitions in practice. It gives insights into where undertakings have the possibility to address climate change risks in ORSA and provides examples using mock non-life and life companies to help undertakings design the steps for the materiality assessment and run climate change scenarios.*

*The concrete case studies for materiality assessment of climate change scenarios included in the guidance can help lower implementation costs for insurance undertakings, in particular small and mid-sized ones, taking into account the size, nature and complexity of climate change risk exposures."*

### Report on voluntary disclosures under SFDR

The three European Supervisory Authorities (EIOPA, EBA and ESMA) have published their first annual report on the extent of voluntary disclosure of principal adverse impact under the Sustainable Finance Disclosure Regulations (SFDR).

Some notable observations from the report include:

- Compliance levels vary markedly across respondents. But overall, disclosures to date lack detail. This is expected to change on disclosures made for the 2022 reporting period.
- Disclosures on the degree of alignment with the Paris Agreement are often either lacking or too vague.
- There was also a lack of disclosure around possible adverse climate impacts due to investment decisions.

The report also makes recommendations to national supervisors on supervision expectations of market participants.

## EIOPA guidance on customer's sustainability preferences under IDD

EIOPA has published guidance on integrating customer's sustainability preferences in the suitability assessment under the Insurance Distribution Directive ("IDD").

The guidance covers:

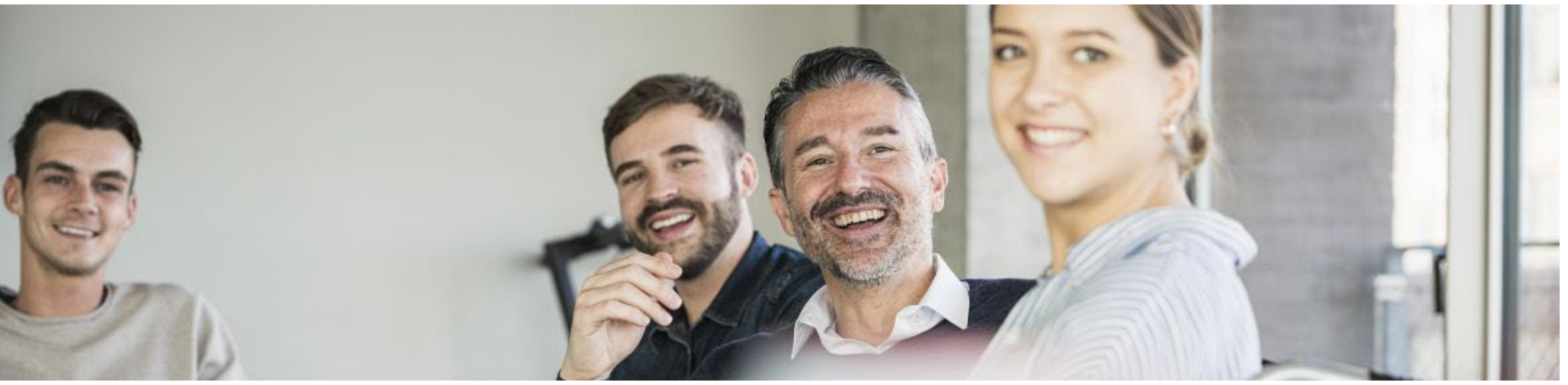
- Assisting customers better understand their sustainability preferences and investment choices;
- Collection of data on preferences;
- Matching of preferences with suitable products;
- How to ensure suitability of insurance-based investment products;
- Training and competence expected of insurance intermediaries and professionals who provide advice on insurance-based investment products.

## Disclosures for fossil gas and nuclear energy investments

During September, EIOPA, in conjunction with the EBA and ESMA, delivered a final report to the European Commission regarding the disclosure of financial products to investments in fossil gas and nuclear energy activities under the Sustainable Finance Disclosure Regulations ("SFDR").

The aim is to assist investors in making informed decisions. In particular, an explicit "yes/no" question is expected to be added to financial product templates, identifying whether the product intends to invest in such activities.

The European Commission will now scrutinise the regulation and include an expected application date.



# CBI Updates

## Inflation

Inflation featured strongly in communications from Governor Gabriel Makhlouf during Q3 2022, having been touched upon in his

- **blogpost of 25th July on "Fiscal Policy and planning for resilience"; and**
- **address to the Dublin Chamber of Commerce on 14th September GM.**

In both communications the CBI's and the ECB's aim to dampen inflationary pressures and to achieve their target of 2% inflation over the medium term are reiterated.

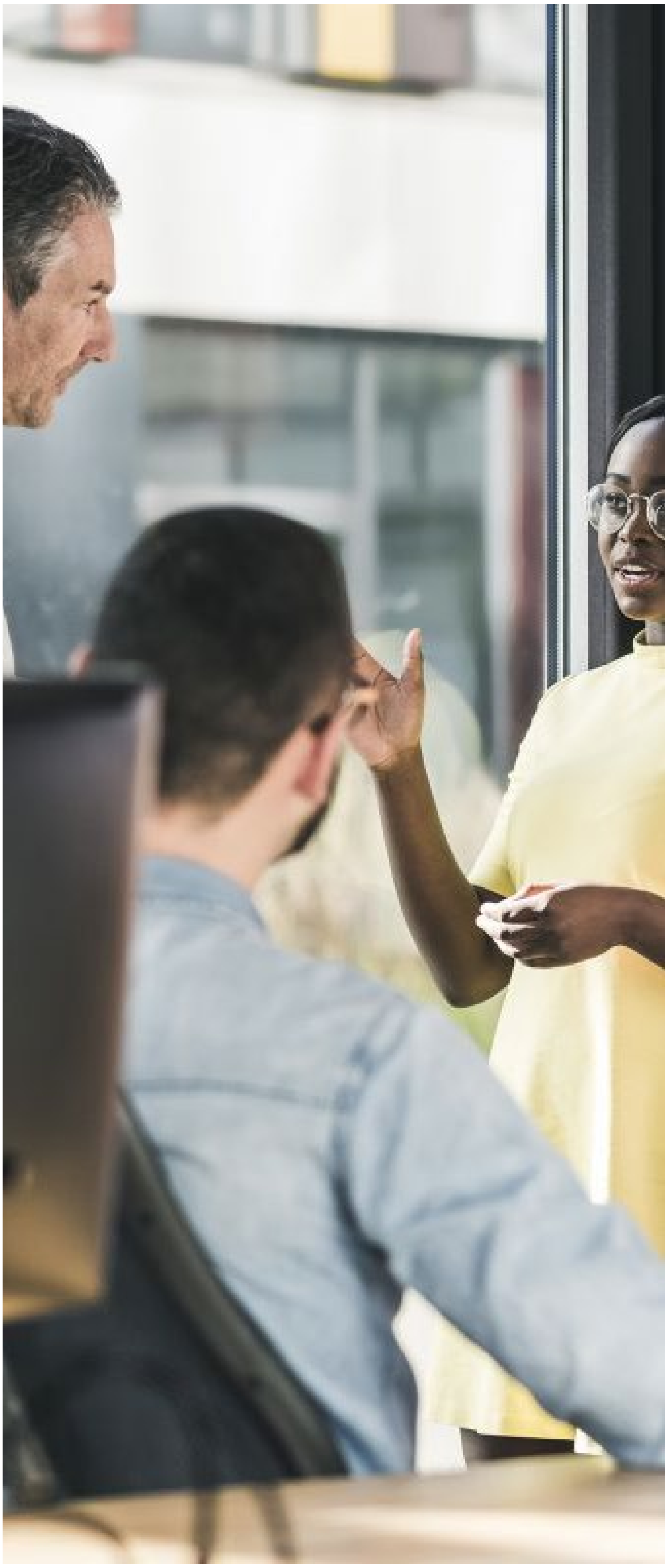
The June headline rate of inflation was 8.6% while "core" inflation was 3.7% (i.e. with the more volatile components removed). In August 2022 headline inflation rose to 9.1% while core inflation was 4.0%, consistent with initial price pressures in energy and commodities having spilled over into many of the everyday good and services we consume.

The impact of high inflation and heightened uncertainty on consumer and business confidence was called out.

The July blogpost contained a useful graph on the CBI's central forecast of inflation along with a downside scenario. These showed annual average rates of inflation of 7.8% in 2022, 4.2% in 2023 and 2.1% in 2024; and a downside scenario with rates of 2022, 7.1% in 2023 and 2.9% in 2024.

Overall the expectation is now toward a slower growth and a higher inflation profile through 2023 than the CBI had previously expected.

The full blogpost can be found here while the address to the DCC can be found here.



## Insurance Quarterly Newsletter – September 2022

The September issue was published on 16 September and can be read here.

The key topics & themes within this were:

- Sustainable insurance;
- Digitalisation in insurance;
- Outsourcing and underwriting by MGAs;
- Operational resilience and the potential for consumer detriment;
- CP150 – Guidance on IGTs;
- EIOPA Consultation on Governance in Third Country Branches, launched on 1 August.

Several of these items are discussed further in this newsletter.

## CP150 – Guidance for (Re)insurance Undertakings on Intragroup Transactions (IGTs) and Exposures

**The CBI have launched a consultation to seek stakeholders' views on proposed guidance in this area.**

The CBI recognises the benefits to companies of intragroup financial links, while also recognising that these may lead to increased concentration and other risks, including a potentially heightened risk of inadequate governance and/or recording of intragroup transactions. While overall responsibility for oversight and management of significant IGTs and Risk Concentrations is with the Group, the CBI believes the strong and robust oversight and monitoring is also required at local entity level.

The aim of the Guidance is to provide clarity on the Central Bank's expectations with regard to intragroup transactions and exposures of (re)insurance undertaking supervised by the Central Bank and in doing so to promote a level playing field in this regard.

The proposed Guidance focuses on

- Governance and Risk Management for IGTs generally;
- Key exposures (which are the most significant exposures observed by the CBI):
    - Intragroup assets
    - Intragroup reinsurance
    - Cash pooling/treasury function arrangements

While the guidance is addressed to (re)insurance undertakings authorised by the CBI which are part of a group, the guidance explicitly states that this includes captives and third country branches authorised by the CBI.

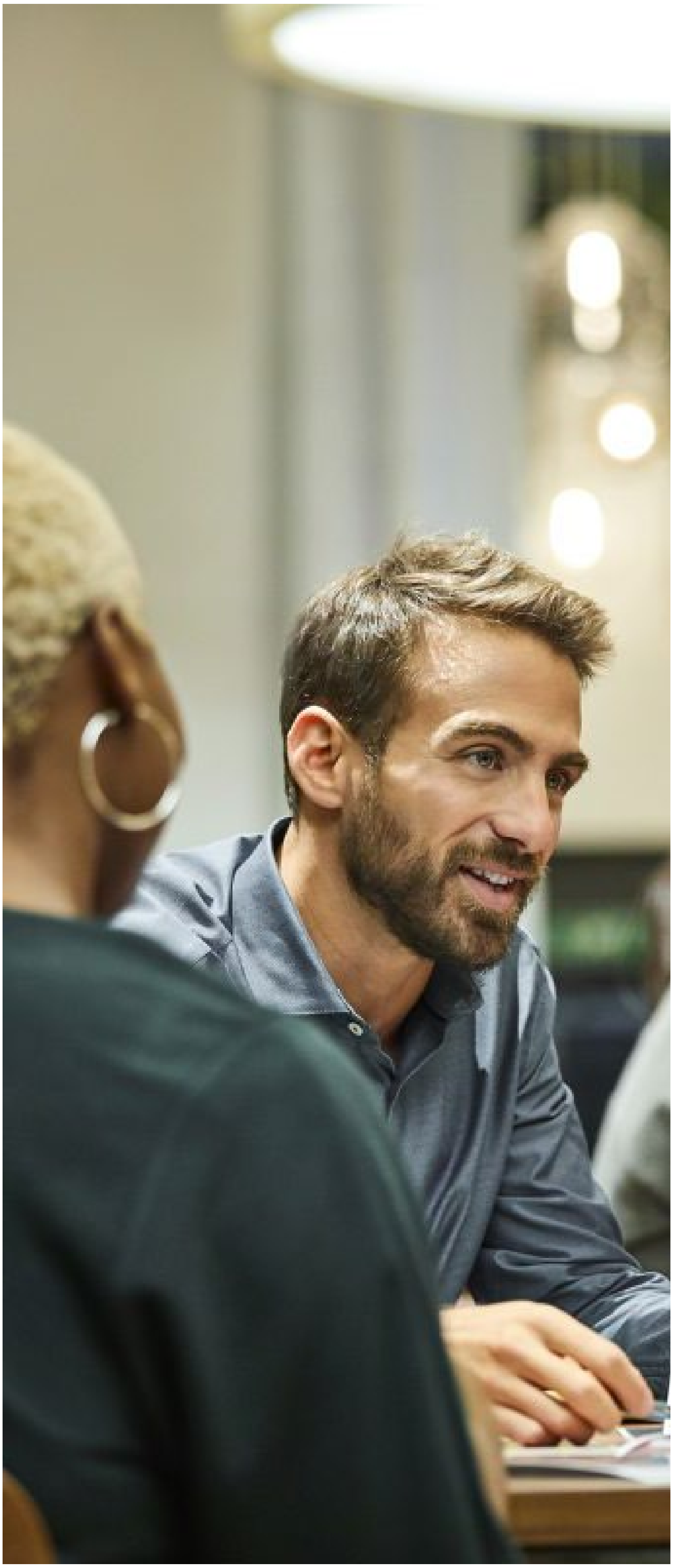
The consultation closed on 22 September.

## Individual Accountability Framework (IAF)

On 28 July the Oireachtas published the Central Bank (Individual Accountability Framework) Bill 2022. The Central Bank will continue to work with the Department of Finance throughout subsequent stages as the legislation progresses through the Oireachtas to enactment. Once the Bill has been enacted the Central Bank intends to publicly consult on the implementation of the IAF.

For further information on IAF/SEAR you might like to read our recent report on companies preparedness, further to a survey carried out by Mazars in conjunction with the Compliance Institute.

Also, an Irish Times article from our Mazars Partner in Financial Services Consulting, Kian Caulwell, may be of interest to readers.



## Fines & Reprimands

### CBI issues record fine to Bank of Ireland

On 27 September, the CBI reprimanded and fined The Governor and Company of the Bank of Ireland ("Bank of Ireland") €100.52m in respect of long-running failings on almost 16,000 tracker mortgage accounts.

This is the largest fine imposed by the CBI to date and surpasses the previous record of €83.3m fine imposed upon AIB back in June.

Key findings from the investigation were that:

- Unclear contractual documentation was issued to customers;
- Ambiguities in contract wordings were not interpreted with the customer's best interests in mind;
- Customer's were not fairly warned about the consequences of switching away from tracker mortgages;
- Unfair complaint handling practices were observed;
- A significant number of operational errors, resulting in consumer detriment, were observed on account of deficiencies in systems and controls;
- Certain customers were wrongfully excluded from the Tracker Mortgage Examination, hence Bank of Ireland failed to 'Stop the Harm' in such cases.

Full details of the CBI's press release can be found here.

### Danske Bank

On 15 September Danske Bank A/S was fined **€1.82m** and reprimanded by the

Central Bank for transaction monitoring failures in respect of anti-money laundering and terrorist financing systems. Three breaches of the Criminal Justice (Money Laundering & Terrorist Financing) Act 2010 (the CJA) were noted.

The three breaches stemmed from the failure by Danske Bank A/S (Danske) to ensure that its automated transaction monitoring system monitored the transactions of certain categories of customers of its Irish branch for a period of almost nine years, between 2010 and 2019.

This is the first penalty that the Central Bank has imposed on a financial institution which is incorporated and supervised outside of Ireland (i.e. in Denmark) but which operates in Ireland as a branch on a passport basis.

The CBI's press release can be read in full here.

### Changes to Russia/Ukraine Regulations

The CBI has a dedicated page setting out details of any new restrictive measures/sanctions adopted in relation to the developing situation in Ukraine.

Updates to the page during Q3 2022 relate to

- details of a package of measures adopted by the EU on 21 July. This package is known as the "maintenance and alignment" package.
- information was provided about the reporting of funds or economic resources located within Ireland, updated on 30 August.

**All firms are expected to take steps to ensure they remain compliant with the restrictions and sanctions.**

### Thematic inspection of MGA governance arrangements

As noted in its newsletter, the CBI have recently conducted a thematic inspection of governance and oversight controls in respect of (re)insurer's use of Managing General Agents ("MGAs") for underwriting purposes. Six firms were inspected but the review outputs provide useful feedback for all insurers.

Some of the key concerns highlighted by the Central Bank include:

- The level of outsourcing procedures in respect of Critical or Important Functions or Activities ("CIFA") were found to be lacking and not always in line with the notification requirements;
- Lack of clear reference to MGA Underwriting risks in the risk framework;
- Lack of Risk and Compliance ongoing involvement in the monitoring of MGAs;
- While initial due diligence assessments were observed in all instances, the documentation and procedures surrounding ongoing due diligence was typically insufficient.

### Outsourcing Registers

The CBI has issued guidance to insurers on completion of the outsourcing register templates. As set out in the Cross-Industry Guidance on Outsourcing, the CBI expects all regulated firms to maintain an outsourcing register. All firms with PRISM rating of Medium-Low or above will be required to have their registers, in respect of 31 December outsourcing arrangements, submitted to the CBI by early October 2022.

The guidance note can be found here.

## Central Bank review identifies under-insurance in the home insurance market

The CBI has written to relevant insurance firms outlining expectations relating to the risks of insufficient home insurance cover.

The 23 September letter follows a Thematic review conducted earlier in the year.

The review revealed that:

- Under-insurance in the home market has now reached 16.5% compared to 6.5% five years ago;
- More could be done to remind consumers of the need to review their sum insured and the consequences of under-insuring.

As such, the CBI have set out expected actions of insurers so as to afford better protection to consumers.

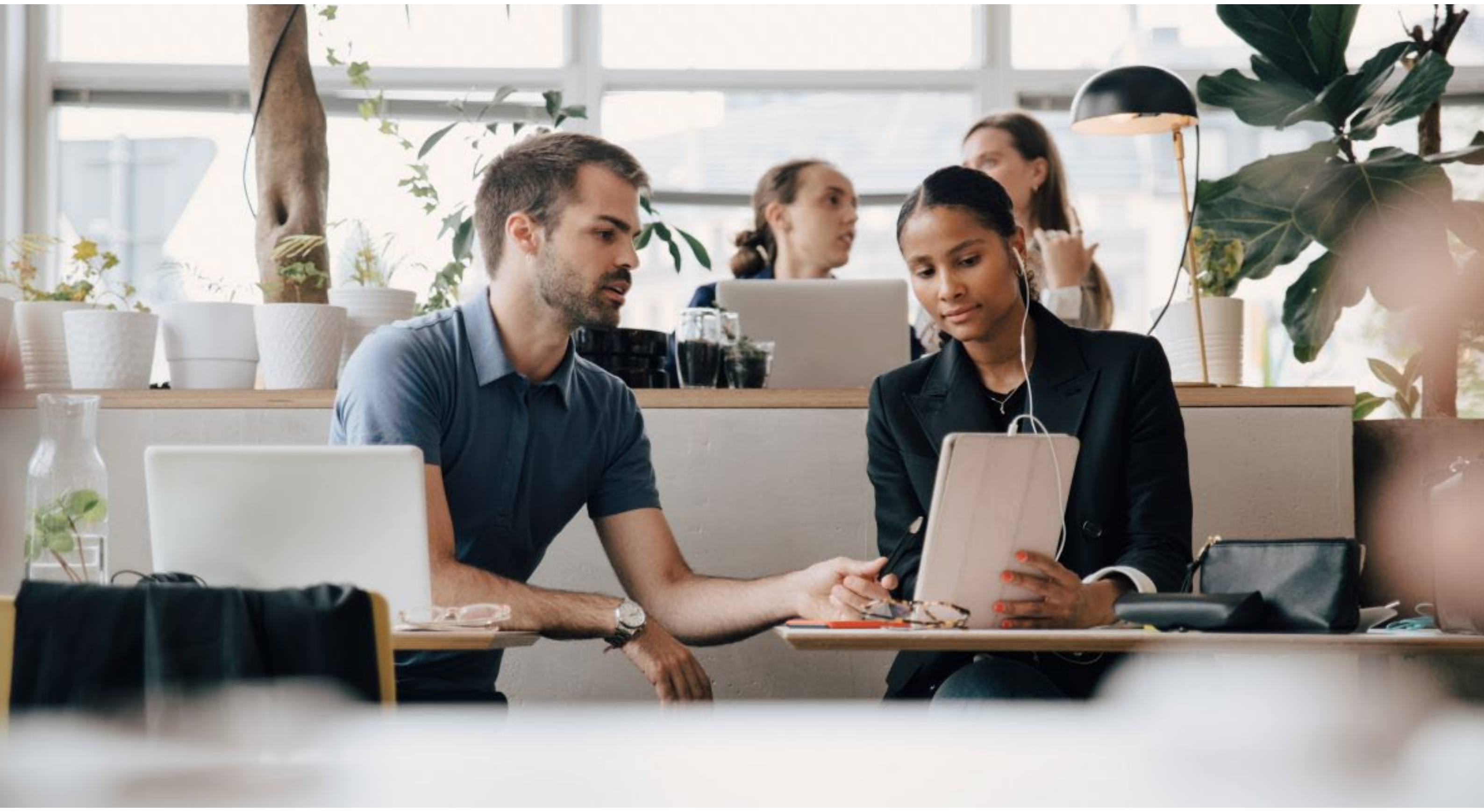
## Consumer Protection Code Discussion Paper

On 3 October, the CBI launched a Discussion Paper with regards to the Consumer Protection Code ("CPC") Review. The paper has been launched in tandem with a survey, inviting views from industry and members of the public alike.

The broad ranging discussion paper covers several themes such as:

- Availability and choice to consumers;
- Acting in consumer's best interests;
- Innovation and digitalisation;
- Pricing practices;
- Informing customers effectively;
- Vulnerability;
- Financial literacy.

The discussion paper engagement runs to March 2023, with formal consultation due in late 2023 and finalisation of a revised framework expected in 2024.



# EIOPA Developments

## EIOPA sets out strategy for 2023-2026

On 30 September, EIOPA set out its strategy for the upcoming years. The key priorities have been identified as:

- Sustainable finance;
- Supporting the opportunities whilst minimising risks of digital transformation;
- Sound, efficient and consistent supervision across the EEA;
- Policy development and delivering high-quality advice;
- Financial stability with particular focus on emerging threats and vulnerabilities;
- Internal governance of EIOPA.

EIOPA have also set out their programme of work for 2023 which includes:

- Integration of ESG in the prudential framework;
- Climate change stress tests;
- Implementation of the Digital Operational Resilience Act ("DORA");
- Developing the regime for the use of AI by insurers;
- Cross-border activity risks;
- Delivering advice on the IORP II Directive;
- Considering the ongoing downside risks of continued high inflation.

## EIOPA consultation paper on governance arrangements in third countries

Also in August, EIOPA launched a consultation relating to a draft supervisory statement on the use of governance arrangements in third countries.

EIOPA's intention is to enhance the supervision of insurer's compliance with EU legislation concerning governance arrangements in third countries. EIOPA has previously challenged insurers on the use of "empty shell" companies and expects there to be appropriate levels of substance in third country entities, in particular around the presence of key-decision makers and function holders.

The consultation process runs until 31 October 2022.

## EIOPA peer review on outsourcing

In July, EIOPA published the report of its peer review on outsourcing. The objective of the review was to identify divergent approaches adopted by national supervisors in a bid to promote a consistent framework.

EIOPA has noted that the level of outsourcing is generally increasing across Europe, particularly in respect of technology. A number of areas requiring further convergence were observed. As such EIOPA will consider conducting further analysis on various topics:

- Outsourcing of delegated authority;
- Definition of 'material development' and 'timely manner' as per article 49(3) of Solvency II;
- Extensive outsourcing to the point that it impacts corporate substance ("empty shell" entities).

### Consultation on supervisory statement on differential pricing practices

In July, EIOPA launched a consultation process on its supervisory statement on differential pricing practices in non-life insurance. Notably from an Irish perspective, this came just after the introduction of the domestic level "price-walking rules" in the home and motor insurance market".

With regards to its consultation, EIOPA has commented: *"While the current EU legislative framework does allow certain differential price practices, such as commercial, marketing and underwriting discounts, EIOPA is of the view that some types of differential pricing practices fail to comply with the applicable framework and lead to the unfair treatment of consumers."*

The consultation process closed on 7 October.

### Supervisory statement on exclusions to systemic events

Between Covid-19 and increasing geo-political instability, the frequency of systemic events have been increasing in recent years. In response, EIOPA have released a supervisory statement aiming to promote convergence of approach across national supervisors.

The statement also aims to consider the interests of both new and existing customers and advocate greater clarity in product wordings. National supervisors are urged to monitor whether insurance manufacturers fully assess the scope of coverage with regards to systemic events. EIOPA also recommends that additional consideration is given to target market's needs, objectives and characteristics with respect to exclusions of such events.

While not all systemic events are fully insurable, EIOPA believes that more can be done to help consumers better assess the risks involved.

### Supervisory statement on management of non-affirmative cyber exposures

EIOPA has also published a supervisory statement in relation to the management of non-affirmative cyber risks (insurance policies that do not explicitly take cyber cover into account).

The statement calls for a top-down approach and risk appetite definition of cyber risks. The statement also highlights the need to review terms and conditions on a regular basis and consideration as to how insurers might communicate changes in cyber coverages to policyholders. Furthermore, traditional war and terrorism exclusions should be reviewed in the context of an increasing digital landscape.

Ultimately, insurers should ensure contracts are unambiguous and exposures should be consistent with each firm's risk appetite. Identification and measurement exercises are required to implement sound cyber underwriting practices.

## Other industry news

### Personal Injuries Resolution Board Bill

On 2 August 2022, the Personal Injuries Resolution Board Bill was published. It aims to increase the remit of the Personal Injuries Assessment Board ("PIAB") and hence the number of claims settled through PIAB. The Bill also provides for a change of name from PIAB to the Personal Injuries Resolution Board ("PIRB") reflecting the body's new statutory powers.

The aim of the Bill is to reduce the time and expense associated with litigation.

Incidentally, the Bill comes just a few days after the PIAB published its 2021 Annual Report which already shows considerable drop in claims. Such claim volumes were down 18% in 2021 compared to 2020, and 31% lower than 2019. Preliminary data also suggests a 42% drop in average claim values since the introduction of new guidelines last year.

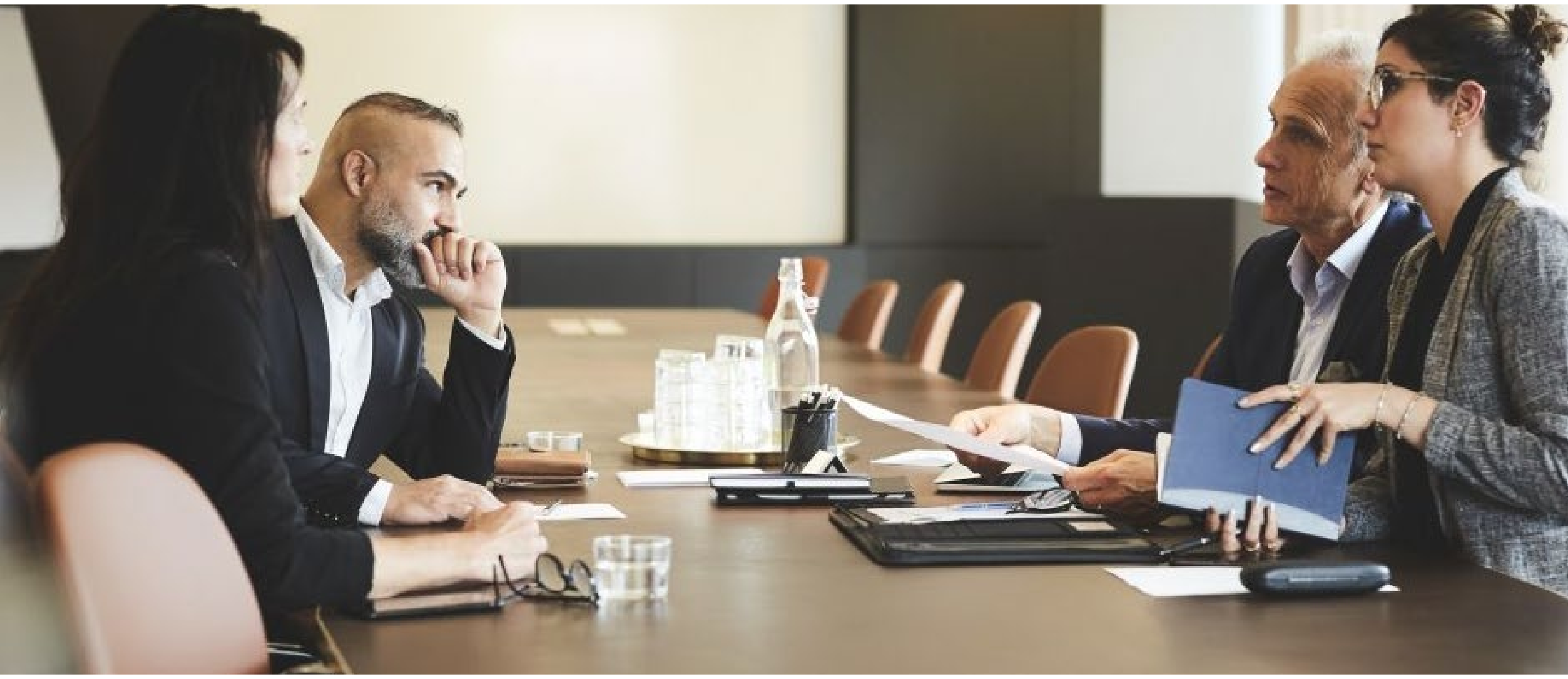
The drop in values have been observed fairly consistently across motor, public and employer's liability classes.

### Insurance Ireland and Broker Ireland Diversity Survey

The second annual diversity survey results were published in September.

The results revealed that:

- 34% of respondents had a D&I strategy in place (27% in 2021);
- D&I was a Board and Executive agenda item for 47% of respondents, up from 39%;
- 19% had a full or part-time D&I resource in place. The comparable figure was 14% in 2021;
- 27% of senior leaders are women.



# Mazars insurance services

Our local team of insurance professionals have the knowledge and expertise to meet your organisation's needs. Click the hyperlinks below for more information or get in touch.

### Actuarial

- Outsourced Actuarial Function services;
- Peer reviews;
- Pricing & underwriting;
- Data analytics;
- Portfolio transfers, mergers and acquisitions.

### Assurance

- External Audit;
- Internal Audit support;
- Outsourced Head of Internal Audit;
- Tax;
- IT.

### IFRS 17

- Transition support;
- Systems development;
- PAA eligibility testing;
- Yield curve assessment;
- Disclosures advice;
- Training programmes.

### Regulatory

- Board training and governance;
- IAF & SEAR preparation;
- GDPR compliance;
- ESG gap analysis;
- CBI licence applications.

### Risk Management

- Risk framework and internal control reviews;
- ORSA support;
- Recovery & Resolution;
- Outsourced Risk Function Services.

### Solvency II

- Capital management;
- Pillar II governance;
- Pillar III support (QRTs, NSTs, SFCR, RSR);
- Third-country branch services.

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