Industry Seminar – 18 November 2015

Insurance Supervision and Policy Division Presentation

Jeremy Quick, Director
Caroline Bradley, Deputy Director

Before I hand over to Caroline, I would like to spend a few minutes talking about the Commission's international engagement around insurance regulation.

I'd like to start with a few words of caution. Firstly, this subject is important but is just one of the many areas where the Commission is accountable; it therefore competes for scarce Commission resources. Secondly, our ability to influence global regulatory outcomes is always going to be limited due to the Bailiwick's relative size and importance. This is not an area where we can appreciably magnify our influence through the Crown Dependencies as Jersey's insurance industry is small and that of the Isle of Man very different to ours.

Nevertheless, we do work for Guernsey as much as we can in the space of international policy.

The key area is naturally the International Association of Insurance Supervisors or IAIS. Here the Commission is represented in its own right at the Technical Committee and through its leadership of the captive working group. The latter has allowed the Commission to play a key role in fashioning IAIS policy around captives – a key industry for Guernsey. The IAIS paper on captives was finally agreed by the IAIS EXCO a few days ago. So we can allow ourselves some congratulation for leading this work in IAIS.

With the Bahamas, the Commission also currently represents offshore jurisdictions as a whole on the IAIS EXCO; this being the highest body at IAIS. In this role, we can periodically articulate key views – for example around the extent to which small jurisdictions can implement large scale policy change.

Having said all this, IAIS's current main policy interest is in global capital standards which at least at present have limited interest for us. On the other hand any eventual international capital might well be applied to all insurers and, were that to be the case, it would benefit us to be at the negotiating table.

We do, by the way, regularly participate in IAIS's self-assessment of insurance core principles. This is useful to understand where we are compared to our peers in real time.

The next global body that we are active in is the Group of International Insurance Centre Supervisors (GIICS) – which contains 19 smaller offshore jurisdictions. This is a discussion and peer training group which allows us to understand how peer regulators undertake the sort of specialised insurance business that Guernsey engages in. For example over the last year we have considered cat reinsurance and financial stability, the regulatory approach to captive company take-overs, the new UK Insurance Act and its impact on captives and so on. As most business is conducted through con calls or on-line and as we tend to meet in London, GIICS is not burdensome. GIICS is also the main electing body for the IAIS EXCO seats.

We also try to keep up bilateral international contacts for policy purposes. This is helped by our presence at IAIS and GIICS – our peers at least know who we are and what we do. One bilateral link is with EIOPA (European Insurance and Occupational Pensions Authority), the EEA standard setter. We may not subject to EIOPA but several of our group insurance companies are. It helps everybody to acknowledge that most large EEA insurance groups have non-EEA host regulators. Another important bilateral link is that with the UK authorities – for obvious reasons. This includes the PRA, the FCA and the regulatory side of Lloyds of London. We also value our US regulatory contacts. An example of this is our interest in investigating whether we can make Guernsey a sort of preferred jurisdiction for cross-border re-insurance.

These contacts help fill in a gap in our everyday supervision. We might reasonably claim to be expert in captive regulation but we have relatively few general or life companies of any size here. This means peer comparison is difficult. So the more we can understand how regulators with larger constituencies supervise their firms, the more we can ensure that our approach is in line with international norms.

Finally, we play our part as global good citizens. For example we are currently supporting the development of captive supervisory standards in a third party jurisdiction, funded by the Commonwealth Secretariat.

I hope I have given you some idea of the Commission's activity in this area. If we were to become too absorbed in this area – which is easy given the inherent interest and glamour of the global issues under consideration – then we would not be able to undertake our other critical tasks, not least everyday supervision. On the other hand, if we were to never leave Guernsey, both we as supervisors and the Guernsey insurance industry as whole would eventually suffer. I hope therefore that we have got the balance right. As is commonly said, you need to at the table to ensure that you are not on the menu.

Thank you for listening. I will now hand you over to Caroline.

Thanks Jeremy and good afternoon everyone.

Slide: Agenda

Here is the agenda for today's presentation. Firstly, I want to review what we have been up to during this year and report on what we have achieved; then I would like to discuss some of the statistics and what they may tell us about the current state of the insurance sector and finally, look forward to see what we have planned for 2016.

Slide: Review of 2015 Activity

So here is a list of the main items I want to cover whilst reviewing our 2015 activity – I won't read it out but as you can see there is a fair amount to get through so I will move straight on.

Slide: Solvency Framework

So, beginning with the solvency framework; which was by far the biggest insurance policy matter we have dealt with over the past few years. The framework was implemented on 1 May and I would like to thank GIIA, especially the Regulatory and Technical Committee for their cooperation in finalising the implementation. We held training sessions for insurance managers in April which were extremely well attended and flushed out some interesting questions at a practical level from the people who will actually have to complete the spreadsheet. We allowed until 31 August for applications for transitional relief, for which we did not receive very many at all, although we have dealt with a large number of queries over implementation for specific firms with specific issues and also with a number of requests for regulatory adjustments. A few of the more eagle eyed amongst you have also spotted one or two errors or ambiguities in the spreadsheet which will be corrected or clarified when we release the next version.

During the period since implementation we have been collating all of the questions and comments we have received in order to ensure that we are consistent in our responses and also with the intention of issuing an FAQ type document which will hopefully assist going forwards. We also want to see if any practical difficulties keep recurring so that they can be addressed within the FAQ document. We have also received feedback from GIIA on several issues that had been raised by the members since the implementation of the rules.

Taking all of the issues, questions, comments and errors into account we hope to issue the amended spreadsheet and the FAQ document early in the New Year.

Slide: Thematic Work

Turning now to our thematic work; this is an integral part of our risk based approach which enables us to monitor low impact firms in a proportionate but effective manner.

During May and June we conducted a review of insurance managers' client take on procedures – I must stress that this was not AML related but more about the Manager's understanding of the client and the business. This was, I'm afraid, prompted by a number of applications we received which were of a poor quality and where it appeared that the Manager did not actually fully understand the rationale for the business. This became evident because the business plan contained large sections which were simply copied from the client's website and because each time we asked a question the Manager had to revert to the client for the answer.

We published the thematic report in July and I am pleased to say that we did not find any serious issues and we did comment on those areas of good practice that were found. I would encourage you all to read the report and consider if the issues raised apply in your organisation.

One matter I would particularly draw to your attention is that there were a small number of cases of clients switching Manager with the receiving manager making the assumption that a company must be ok if it is already licensed by the Commission. Please don't make that assumption as it is still incumbent on the receiving Manager to undertake full due diligence. There might be a very good reason why the outgoing manager wants to terminate the relationship so don't always assume that it is the client that wishes to move. A client that falls into your lap without any effort on your part may suggest a client that is desperate to move for the wrong reasons.

Thank you to the Managers who participated in the thematic work and to our two industry experts who worked on the thematic with us. Ideas for future thematic work include: looking at controls around the completion of solvency workbooks or at governance around the underwriting process – I am not sure we will get to these during 2016 as we have other thematic work on banks and conduct to fit in as well.

Slide: Embedding PRISM – themes and findings

Last year we reported to you on the implementation of our risk based supervision framework, Prism and you may recall that the insurance team was the first to implement this framework.

Low impact firms – which would include pure captives, for example, are now mainly dealt with on a reactive and thematic basis and now that the online submissions portal is up and running annual returns from those companies will be automatically assessed for certain key risk indicators. Where an indicator is triggered you may find that we will revert to you for further information.

We have now completed in depth reviews of a number of high, medium high and medium low impact firms and have found the process to be beneficial from a supervisory perspective in really understanding what makes a firm tick. The firms involved have all embraced the process constructively and we hope that they have also found it useful and not too onerous.

There are a number of themes emerging from the risk assessments that we have carried out this year.

In relation to Corporate Governance the findings have generally been good in relation to the balance of the board and the level of oversight and challenge provided by the board to senior management. Remuneration policies are generally appropriate and not overly dependent on business being generated. In a minority of cases we have identified key man risk, especially in smaller commercial insurers.

In relation to companies that are part of larger groups the level of group influence is evident – whether in the systems and controls or in the presence of group representation on the board. This is not in itself a problem providing that the Guernsey entity retains sufficient level of engagement to ensure that local issues are not overlooked. Fundamental issues such as business models are often established at Group rather than local level but it is essential that the Guernsey firm understands the group model and their contribution to that model. Where functions are outsourced to other parts of a group the Guernsey board must retain sufficient oversight of that function by implementing effective systems of review and audit.

Technology is playing an increasing role for many companies and we have observed that issues can arise when a company fails to keep pace with developments, both in internal systems for management information and in its distribution networks.

A key element of our risk assessment centres round the business model and strategy of the organisation. In cases where a firm is offering a niche or specialist product then competition is the biggest threat to their business because they do not have the ability to diversify if their core market becomes unsustainable. It is inevitable that a profitable line of business will attract competition and firms need to plan ahead to deal with that – whether to compete with cost cutters or to sit back and wait for them to fail if they feel the rates are unsustainable.

The banking and insurance teams are continuing to integrate and this year the banking supervisors have embarked on an IAIS related course in insurance supervision. They will of course then need to get some practical experience but they should be able to transfer their experience in prudential supervision and their existing skills in risks such as governance and conduct to the insurance sector. So this will leave us better resourced in terms of insurance supervision in the future.

Slide: Engagement with other regulators

I wanted to say a little bit about our engagement with other regulators. Whilst this is useful to us in gathering information and understanding more about group issues it is also hopefully beneficial to the reputation of Guernsey. In the same way that, as Jeremy outlined, our international work it helpful to the profile and reputation of Guernsey, so too is our attendance at supervisory colleges. We can underline our credentials as a competent and cooperative supervisor by engaging with other regulators on an equal footing. It is also an opportunity to benchmark ourselves against other regulators by observing their supervisory processes.

During the year the supervisory team liaised with other regulators as appropriate whether by telephone or e-mail or attending supervisory colleges where relevant. We attended two colleges and had bilateral meetings with two other regulators. Exchange of information is done on the basis of MOUs, either the IAIS MOU, bilateral MOUs with other supervisors or firm specific MOUs.

We are starting to see the Group-wide supervisors developing their approach to group supervision and therefore we expect the level of interaction to continue to increase.

Slide: Transfer of functions to Authorisations Unit

Turning now to the Authorisations unit. This unit was set up earlier this year and we are grateful to John Dunford, who is now Deputy Director of that unit, for joining us today to deal with any questions you might have on this subject.

All new applications are now dealt with by our dedicated Authorisations team so you should contact them in relation to any potential client meetings or the application process. The supervisory team also remain happy to meet with potential clients if necessary but your first port of call should be the applications team and they will assess whether we need to be involved. The unit has full authority to approve applications but they will seek input from the supervisory divisions if there are any particular issues or if the application raises an issue of policy. Once licensed the company then comes under our supervision.

All PQs and new director or controller appointments are also dealt with by the Authorisations team and they will also deal with other items requiring formal Commission approval such as a change of name, auditor, or year end. Migrations in or out, conversions and surrenders will also fall under the Authorisations unit. They will refer to the supervisory divisions as necessary, particularly for anything involving a firm that is anything other than low impact.

Also, importantly, the unit is home to the helpdesk on 733420 for the online portal so you can call them if you have any issues around any of the online services and they should be able to assist you.

So what is the role now for the supervisory division? Well, as I said, we deal with the ongoing supervision of each licensee, this involves; business plan changes, annual returns, modifications to solvency rules and any other waivers that you may seek, breaches and any other general enquiries and also from time to time, firms that find themselves in difficulties. We also deal with policy areas such as the implementation of international standards.

Slide: IAIS Captive Paper

During this year we have also concentrated some resources on getting the IAIS Captive Paper finalised and adopted after three years of work on our part in leading the drafting group. It was overtaken on the agenda in 2014 by the huge amount of work on solvency and capital standards that the IAIS was working on. Having got it back onto the agenda this year we wanted to make sure we saw it through to adoption.

The paper went to the Technical Committee in June 2015 for approval to go to public consultation. The consultation then took place during July and August. Comments were received from 12 parties, 5 of whom were supervisors and the rest were firms or industry bodies. After amendment to take into account some of the comments the paper was re-presented to the Technical Committee in September and received approval. The final process was adoption at the Annual Meeting which has just happened last week and the paper will therefore be published shortly on the IAIS website.

This is an important piece of work as it helps to establish captives as legitimate insurance vehicles and Guernsey is seen as the expert jurisdiction in this area by our peers at the IAIS.

Slide: IAIS Self-assessment and Peer Review

As part of our preparation for any external assessments of the jurisdiction we are committed to taking part in the IAIS self-assessment and Peer Review process which, this year has covered the ICPs listed here.

I am pleased that we received ratings of largely observant in relation to ICPs 9, 10 and 11 which cover supervisory measures. ICP 9 deals with on and off site reviews and information gathering powers, ICP 10 deals with preventive and corrective measures such as for example, the imposition of licence conditions or restrictions on writing new business. ICP 11 deals with enforcement powers.

We await the results of the self-assessment of ICPs 18 and 19 which deal with the regulation of intermediaries and conduct of business by both intermediaries and insurers. We had hoped to have the results of this by now but the IAIS is still working through the results as so many jurisdictions took part in this assessment.

Our self-assessment of ICPs 14-17 was submitted in October based on our new solvency rules which came into effect on 1 May. Results of these self-assessments are not expected for several months.

Slide: Statistics

So, now let’s have a look at some recent statistics.

For the year ended 31 December 2014 the market remained fairly steady and there was a slight growth in written premiums.

We did see a slowdown in new business during the first half of 2015, however, applications have begun to pick up again in more recent months, indeed October was the best month so far this year. For the period to 30 September there was still net growth of 9 entities with 51 new entities licensed or authorised.

Slide: Statistics (continued)

This slide shows the trend in new licences issued. As you can see there was a drop earlier in the year but this has recovered slightly although not quite back to previous levels.

ILS business still accounts for over half of new cells and there are also a number of After the Event legal expenses cells this year. Other notable licences issued this year include a substantial new reinsurer and a company writing sports risk.

We are aware of several enquiries in relation to pension longevity risk and we hear that there was great interest generated by the Guernsey Finance event in London in October which we hope will come through during the course of next year.

Slide: Looking ahead to 2016

So looking ahead to 2016, firstly, I am sure you will be pleased to hear that there are no major policy developments planned for the year as far as insurance is concerned – I can assure you that is also a relief to us!

Slide: Embedding to solvency framework

We need to embed the new solvency framework and, as I already mentioned, we will issue FAQs and updated spreadsheet in early 2016. We will undertake a more comprehensive review in 2016 once we have the bulk of the annual returns from December year ends to analyse. This will inform any future refinements in the solvency framework and of course we will discuss this with GIIA.

Slide: Annual return regulations

Annual return regulations will need to be reviewed in due course to reflect the reality of the new online submissions requirements. When you come to submit online you will notice that some of the items that you currently submit are no longer required but please don't worry about that, we have been able to dispense with some items which we feel are no longer necessary. The regulations will need to catch up in due course but such secondary legislation will need to wait until after the revision of laws. As I mentioned earlier, to a large extent the returns for low impact licensees will become automated and the system will alert the supervisor if one of the key risk indicators that we have set has been triggered.

Slide: Corporate Governance

The corporate governance code will now become an annex to the finance sector code. We have discussed and agreed this with GIIA but need to ensure that we follow the correct process for amending the finance sector code and therefore will update you on the timetable for this when we have it finalised. We will implement for financial years beginning on or after an agreed date so that no company should be dealing with two separate codes in one financial year.

Slide: IAIS Developments

We of course also need to keep an eye on developments at the IAIS. Their roadmap of activities for 2016 includes various capital standards aimed at Internationally Active Insurance Groups or Systemically Important Insurers. There is of course always the danger that these standards – once established, will filter down to apply to other insurers. The ComFrame continues to develop in conjunction with the capital standards and with ongoing work on updating the ICPs. Recovery and resolution is also on the agenda for 2016 together with evolving thinking on group supervision and further work on how proportionality is woven throughout the ICPs.

Although we don't anticipate any major issues to affect us during 2016 we will need to monitor the ICP updates and this will also form part of our preparation for an IMF visit, not because we intend to plug every gap but because we need to be aware of where those gaps are in order that we can arrive at sensible decisions about whether they are relevant for us.

Slide: US – Qualified Jurisdiction

Earlier this year, at the request of GIIA, we began to explore the possibility of Guernsey applying for Qualified Jurisdiction status in the US as a means of mitigating the collateral requirements often imposed on non-US reinsurers.

The process is based on a model law on Credit for Reinsurance which was developed in order to reduce the barriers to entry caused by the collateral requirements imposed in the US.

We made initial contact with the NAIC to find out a bit more about the process and now have some idea of what might be involved, in particular that we would need a reinsurer to work with us as part of the process. There would undoubtedly be a lot of work involved both for the Commission and any reinsurer involved and the benefits are not automatically applied even if qualified jurisdiction status is granted.

It is not yet clear that the industry demand or appetite exists for us to proceed with this. I will leave that one for you to think about but the Commission is happy to explore further in the future should you wish to do so.

That concludes my remarks and I will now take questions along with Jeremy and John.