IDEAS | PEOPLE | TRUST

Insurance Regulatory eBulletin

Round up of regulatory developments in May 2024

BDO

WELCOME TO OUR INSURANCE REGULATORY EBULLETIN

As we move into meteorological Summer, welcome to this May 2024 edition of our Insurance Regulatory eBulletin. This aims to keep you updated with significant regulatory developments, during the month, and their implications across the insurance sector.

The date for the next General Election was announced on 22 May. This had the effect of ceasing publication of any major regulatory consultations or significant final rules, from this date until after the election. Therefore this month is slightly lighter than some recently. Nevertheless, this edition contains details of some important regulatory announcements.

The PRA has issued its Policy Statement in respect of insurance branches. This includes a new statement of policy, detailing the authorisation and supervision of third-country insurance branches, which are foreign undertakings authorised to operate in the UK. It also outlines when a subsidiary is more appropriate than a branch. There was a speech by Emily Shepperd, of the FCA where, amongst other topics, she emphasised the need for the broking community to demonstrate value in commission design. This should be read in the context of the action taken in respect of GAP insurance. This edition also notes that the FCA have permitted several firms to recommence sales in this area, following action to improve fair value.

There has also been guidance from the FCA to the Financial Services market, in the form of separate Dear CEO letters to specific areas of the industry. These set out its expectations regarding the extension to the Consumer Duty coming into force for closed products and services on 31 July 2024. Firms will therefore need to be prepared for this.

I have highlighted certain elements. However, there is much detail included in this eBulletin, referenced to the source documents. I hope you will find this helpful in identifying matters relevant to yourself. Please do not hesitate to contact myself or your usual BDO contact if you have any concerns over any matter highlighted in this update. For more information about our audit, tax and advisory services to the insurance sector, visit our insurance services page.

I hope you enjoy reading this latest update.

ALEX BARNES
PARTNER

+44 (0)7903 891 435
alex.barnes@bdo.co.uk

CONTENTS

PRUDENTIAL REGULATION

THE UK'S DIGITAL SECURITIES SANDBOX: SUPPORTING THE NEXT FRONTIER OF INNOVATION - SPEECH BY SASHA MILLS

On 21 May, Sasha Mills, Deputy Governor for Financial Stability at the Bank, delivered a speech at City Week 2024, titled: "The UK's Digital Securities Sandbox: supporting the next frontier of innovation".

She discussed how support for innovation interacts with clear rules and a commitment to financial stability, as well as opening the next frontier for innovation. The Bank and the FCA are consulting on the architecture around the new Digital Securities Sandbox. She also spoke about the Bank's approach to facilitating innovation, particularly in areas of finance where there are deep-rooted, historic processes and infrastructure.

BALANCING THE PRODUCTIVITY OPPORTUNITIES OF FINANCIAL TECHNOLOGY AND AI AGAINST THE POTENTIAL RISKS - SPEECH BY RANDALL KROSZNE

On 21 May, Randall Kroszner, an external member of the Financial Policy Committee (FPC) and Financial Market Infrastructure Committee (FMIC), delivered a speech at City Week 2024, titled: "Balancing the productivity opportunities of financial technology and AI against the potential risks".

He discussed the potential of technology and AI for innovation and productivity growth and highlighted the financial stability risks. He differentiated between disruptive and incremental innovation and discussed regulatory challenges in handling these changes. He also emphasised the importance of the FPC and FMIC in considering these issues for their primary and secondary objectives.

PRA BUSINESS PLAN 2024/2025

The PRA has published its 2024/25 Business Plan. This sets out the workplan for each of its strategic priorities to support the delivery of the PRA's strategy, together with an overview of the PRA's budget for 2024/25.

Amongst many initiatives relevant to the insurance industry the following areas were noted:

- providing timings for the implementation of Solvency UK reforms of insurance capital standards;
- the introduction of a new 'mobilisation' regime to facilitate entry and expansion for new insurers from 31 December 2024, similar to the mobilisation stage for new banks. Other improvements to authorisation processes relevant to the insurance industry were also noted;
- plans for stress testing in the insurance industry;
- monitoring and assessing cyber underwriting risk;
- scrutiny of internal models for model drift, both within the industry and within specific firms;
- building on the existing liquidity framework to develop liquidity reporting requirements for insurance firms most exposed to liquidity risk; and
- continuing to monitor threats to firms' resilience, including their growing dependency on third parties, while respecting the principle of proportionality.

UPDATE OF THE MEMORANDUM OF UNDERSTANDING BETWEEN THE BANK AND THE FCA

There has been an update on the Memorandum of Understanding between the Bank and the FCA. This sets out the high-level framework the Bank of England and the FCA will use to co-ordinate and co-operate in carrying out their respective responsibilities.

THE BANK'S APPROACH TO STATUTORY NOTICE DECISIONS FOR USE OF ITS REQUIREMENTS POWERS - MAY 2024

On 23 May, the Bank released a policy statement providing feedback on the consultation regarding its approach to statutory notice decisions for its requirements powers, under the Financial Services and Markets Act 2000, as amended by the Financial Services and Markets Act 2023. The statement outlines the Bank's final policy on decision-making processes related to the powers granted to regulate central counterparties and central securities depositories, ensuring transparency and accountability, and including new obligations such as cost-benefit analysis and innovation facilitation.

The final statement of policy took effect from 23 May 2024.

PS7/24 – SECURITISATION: GENERAL REQUIREMENTS

The PRA has published a policy statement that provides feedback to the responses it received to its consultation paper 'Securitisation: General requirements'. The Policy Statement also contains the PRA's final policy, as follows:

- a new Securitisation Part of the PRA Rulebook (along with consequential amendments to the Liquidity Coverage Ratio (CRR) Part and the Non-Performing Exposures Securitisation (CRR) Part of the PRA Rulebook); and
- an updated PRA supervisory statement 10/18 - Securitised General requirements and capital framework.

The changes resulting from the Policy Statement will come into force on 1 November 2024, subject to the revocation of the Securitisation Regulation and related technical standards. The PRA and the FCA expect to consult on further changes to their securitisation rules in Q4 2024 / Q1 2025, although timings are potentially subject to change.

PS8/24 THE PRA'S APPROACH TO THE AUTHORISATION AND SUPERVISION OF INSURANCE BRANCHES

On 23 May, the PRA published a policy statement providing feedback to responses to consultation paper CP21/23. This Policy Statement confirms the PRA's approach to the authorisation of insurance branches. This includes a new statement of policy, detailing the authorisation and supervision of third-country insurance branches, which are foreign undertakings authorised to operate in the UK. It also outlines when a subsidiary is more appropriate than a branch. This policy does not apply to Swiss General Insurers, who are subject to different requirements under the Swiss Treaty Agreement.

CONDUCT REGULATION

POWER BROKERS: HOW TO TRANSFORM INTO THE LYNCHPINS OF THE ECOSYSTEM

On 16 May 2024 Emily Shepperd, the FCA Chief Operating Officer, delivered a speech at the British Insurance Brokers' Association (BIBA) Conference. She discussed how brokers can responsibly use their power and influence the financial ecosystem. She also discussed the need for the industry to take the lead in policing non-financial misconduct, fostering positive work environments, and demonstrating the value of brokers in commission design.

She stated:

“The growth of your market and the premiums you wrote is staggering and shows that at a time when much human-driven expertise is facing an existential threat from automation, there is a healthy demand for the services of brokers”.

"The key to your long-term survival will be maintaining and enhancing that value to your customers and the wider financial ecosystem. Remember, the wolves were banished from Yellowstone for the perception that they were cavalier predators."

She also discussed the FCA's initiatives to lessen the regulatory load on brokers, especially in cases when insurance is arranged through foreign brokers.

FIRMS TO RECOMMENCE GAP INSURANCE SALES FOLLOWING FCA ACTION

On 24 May, the FCA confirmed that several firms have been permitted to recommence their sales of Guaranteed Asset Protection (GAP) insurance, following action by the regulator to improve fair value. In order to resume sales, companies must show that, in compliance with FCA regulations, their GAP products offer fair value to clients. Firms that have resumed sales of GAP insurance have done so with significantly lower rates of commission being paid out to those selling GAP, thus improving value for customers.

DEAR CEO LETTER: IMPLEMENTING THE CONSUMER DUTY FOR CLOSED PRODUCTS AND SERVICES - LIFE INSURANCE

On 16 May, in advance of the Consumer Duty coming into force for closed products and services on 31 July 2024, the FCA published guidance within various Dear CEO letters, including those to Life Insurance firms and to all other firms in regulated sectors of the financial services industry not receiving specific guidance letters. This was with the objective of supporting firms in their final preparations for this deadline.

The letters set out:

- the application of the Consumer Duty, which sets higher standards for retail financial services customers;
- priority issues that are particularly acute or widespread in Closed Products and Services;
- action prompts to ensure firms are prepared for the 31 July 2024 deadline; and
- a reminder, in Annex 1, of the definition of Closed products and Services and an overview of the Rules.

The FCA expects firms' senior management to consider the contents of these letters and take steps to ensure their firm is compliant with the Duty by the deadline.

FCA PUBLISHES PS24/3: CONSUMER CREDIT - PRODUCT SALES DATA REPORTING

The FCA has published policy statement (PS) 24/3 in response to feedback in respect of Consultation Paper (CP) 23/21 which set out proposals for the introduction of three new Product Sales Data (PSD) returns into Chapter 16 of the Supervision manual (SUP 16). This policy statement summarises the feedback received to the proposals and the FCA’s response, as well as setting out the FCA’s final rules and guidance for incorporating the three new PSD returns into SUP 16. Following feedback from firms and subsequent analysis, to reduce the heightened burden of reporting on smaller firms, the FCA have decided to raise the threshold for firms to report PSD to £500,000 in outstanding balances and/or new advances to £2m.

ADDENDUM TO CP24/6

On 29 May, the FCA published an addendum to its consultation paper CP24/6 on regulatory fees and levies in relation to rates proposals for 2024/25. Following feedback received on the CP, the FCA have expanded Table 3.3, which shows the data used to estimate 2024/25 periodic fee-rates.

REGULATION ROUND UP

On 30 May, the FCA published its monthly Regulation Round-up. In addition to various topics, noted either last month or above, this noted, the following:

- Impact of the general elections on FCA activities. The essential business that the FCA carries out will continue and be publicised as normal. However, the FCA will not be publishing any major consultation or significant final rules during the election period and while Parliament is dissolved.
- Latest Authorisations Operating Service performance showing 10 metrics are green, 6 are amber and none are red. Some 98.1% of applications across all metric areas were determined within the statutory deadline.

EIOPA

We continue to monitor EIOPA's activity and draw your attention to it, where we believe it to be necessary or helpful. This will, we hope, assist those firms operating in the EU.

Items of possible interest this month are as follows:

EIOPA-BOS-24/139 REPORT ON THE DIGITALISATION OF THE EUROPEAN INSURANCE SECTOR

EIOPA has published a report that assesses the level of digitalisation in the European insurance sector. This presents the results of a market monitoring exercise, as well as findings from a Eurobarometer survey of customer attitudes towards digitalisation. Some of the key findings include, among other things:

- the level of digitalisation among European insurers is varied and, in most cases, still at an early stage;
- digital-only distribution channels still lag well behind physical or hybrid ones. This is especially true for life insurance products where consumer prefer in-person meetings even though online tools are also used to compare products or get more information about certain offers; and
- telephone calls, emails and face-to-face meetings are the most popular communication channels for the moment, but the use of chatbots is expected to rise significantly, not least due to the emergence of generative AI.

The report highlights that approval from compliance and risk functions is often not required before high-impact AI is rolled out at firms. While board sign-off was required 65% of the time, approval from compliance was needed just 35% and risk 30% of the time.

EIOPA RECOMMENDS IMPROVEMENTS IN THE SUPERVISION OF THE 'PRUDENT PERSON PRINCIPLE' FOLLOWING PEER REVIEW

On 2 May, EIOPA conducted a peer review on the supervision of the Prudent Person Principle (PPP) under Solvency II, with a focus on the supervision of investments in non-traditional and complex assets like derivatives in unit-linked and index-linked contracts.

The PPP is set out in Article 132 of the Solvency II Directive. Under the principle, which provides a safeguard against concentration risk, insurers are required to invest only in assets where they can properly identify, measure, monitor, manage, control and report the risks.

EIOPA has identified 15 areas related to PPP supervision and has issued 49 recommended actions to 22 National Competent Authorities (NCAs) to strengthen their oversight and safeguard policyholders' interests. The recommendations included developing internal guidance, improving supervision of derivatives, developing risk indicators on the PPP to implement a data-driven supervision, setting specific expectations for insurers in unit-linked and index-linked contracts, and addressing supervisory tools, portfolio security, asset-liability management, valuation of investments, and the control of the risks of underlying assets for unit-linked and index-linked contracts. EIOPA will monitor NCA compliance and consider the findings for future efforts in supervisory convergence.

JC 2024 22 ESAS RISK UPDATE: RISKS REMAIN HIGH IN THE EU FINANCIAL SYSTEM

The European Banking Authority (EBA), EIOPA, and European Securities and Markets Authority (ESMA), collectively known as the three European Supervisory Authorities (ESAs) have issued their Spring 2024 Joint Committee Update on Risks and Vulnerabilities in the EU Financial System. The risk update shows that risks remain elevated in a context of slowing growth, an uncertain interest rate environment and ongoing geopolitical tensions. The prudential and liquidity positions remained solid in 2023, with insurance solvency ratios well above 200%. Defined benefit occupational pension schemes (IORPs) improved their financial position.

EIOPA INSURANCE RISK DASHBOARD FLAGS MARKET RISKS FOR INSURERS AMID MARKET VOLATILITY AND DECLINING REAL ESTATE PRICES

EIOPA has published its May 2024 Insurance Risk Dashboard, which shows that risks in the EU's insurance sector are stable and overall at medium levels, with pockets of vulnerabilities stemming from market uncertainty and potential risk in the real estate sector.

EIOPA'S IORP RISK DASHBOARD HIGHLIGHTS MARKET RISKS AS KEY CONCERN FOR OCCUPATIONAL PENSION FUNDS

On 2 May. EIOPA published the second edition of its Occupational Pensions Risk Dashboard, which shows that the exposure of IORPs to market and asset return risks remains at a high level due to market volatility and real estate market vulnerabilities. Macro risks are at a medium level with macroeconomic indicators showing signs of positive developments such as a decline in forecasted inflation and improvements in the GDP growth outlook. Liquidity risks are also at a medium level but show a decreasing trend compared to the previous quarter, driven by developments in derivative positions. The medium-level reserve and funding risks are unaffected, but the defined benefit IORPs' financial circumstances have slightly deteriorated due to reduced interest rates. Currently, all other risk categories are rated as medium; it is anticipated that the risk level for cyber and digitalisation concerns would rise throughout the course of the next year.

EIOPA PUBLISHES MONTHLY TECHNICAL INFORMATION FOR SOLVENCY II RELEVANT RISK-FREE INTEREST RATE TERM STRUCTURES - END-APRIL 2024

On 6 May, EIOPA issued technical information on the relevant risk-free interest rate term structures (RFR) with reference to the end of April 2024. The RFR information has been calculated based on the Technical Documentation. EIOPA publishes technical information relating to RFR term structures monthly via a dedicated section on EIOPA's website together with other related information.

MONTHLY UPDATE OF THE SYMMETRIC ADJUSTMENT OF THE EQUITY CAPITAL CHARGE FOR SOLVENCY II - END-APRIL 2024

On 6 May, EIOPA published the technical information on the symmetric adjustment of the equity capital charge for Solvency II at end of April 2024.

CORPORATE GOVERNANCE

FRC PUBLISHES NEW TECHNICAL ACTUARIAL STANDARDS FOR COLLECTIVE MONEY PURCHASE PENSIONS

On 24 May, the Financial Reporting Council (UK) (FRC) published version 1.0 of Technical Actuarial Standard 310: Collective Money Purchase Pensions (TAS 310). This follows a consultation to ensure developments in this emerging area of work are proportionately reflected. TAS 310 allows for the different considerations for actuarial work in relation to collective money purchase pension schemes, compared to defined benefit or defined contribution pensions. The new Standard includes requirements in relation to assumptions and modelling, as well as the provision of advice on assessments of scheme soundness, scheme valuations and setting actuarial factors.

UK GOVERNMENT: SETS OUT FRAMEWORK FOR DEVELOPING SUSTAINABILITY REPORTING STANDARDS AND PROVIDES IMPLEMENTATION UPDATE ON SUSTAINABILITY DISCLOSURE REQUIREMENTS

On 16 May, the UK Government published its framework to assess the suitability of the International Financial Reporting Standards (IFRS) S1 and IFRS S2 for endorsement in the UK. If this process concludes with an affirmative endorsement decision, it will result in the creation of the first two UK Sustainability Reporting Standards (SRS), which would be based on IFRS S1 and IFRS S2.

Once the assessment process is complete, and subject to an affirmative endorsement decision, the FCA will be able to use the UK's standards to introduce requirements for UK-listed companies to report sustainability-related information to their investors, subject to a consultation process.

INFORMATION COMMISSIONER'S OFFICE

We continue to monitor material being issued by the Information Commissioner's Office with a view to highlighting high-level matters that may be relevant to readers. There were no relevant matters identified this month.

ENFORCEMENT ACTION

PRA / FCA REGULATORY FINES ROUND-UP

We have identified key relevant enforcement action during May and in this respect, fines announced by the PRA / FCA were:

HSBC	The FCA has fined HSBC UK Bank PLC, HSBC Bank PLC, and Marks and Spencer Financial Services plc (HSBC) £6,280,100 for failures in its treatment of customers who were in arrears or experiencing financial difficulty. The FCA considered HSBC's remedial and redress scheme when determining its penalties. HSBC also agreed to resolve the lawsuit and received a 30% cut on the financial penalty, which would otherwise have been £8,971,600.

CONTACTS

EXTERNAL AUDIT

ALEX BARNES
Partner & Head of Insurance Audit
alex.barnes@bdo.co.uk

GEETA JOSHI
Partner
geeta.joshi@bdo.co.uk

GILES WATSON
Partner
giles.watson@bdo.co.uk

TOM REED
Partner
tom.reed@bdo.co.uk

RUPERT LIVINGSTONE
Principal
rupert.livingstone@bdo.co.uk

ADEEL AJMAL
Director
adeel.ajmal@bdo.co.uk

MZ NETYISI
Director
mz.netyisi@bdo.co.uk

INTERNAL AUDIT

CHRIS BELLAIRS
Partner
christian.bellairs@bdo.co.uk

LUKE PATTERSON
Partner
luke.patterson@bdo.co.uk

SAM PATEL
Partner
sam.patel@bdo.co.uk

JOHN OWENS
Director
john.owens@bdo.co.uk

KUDZANAI MUMBURE
Director
kudzanai.mumbure@bdo.co.uk

REGULATORY ADVISORY

MICK CAMPBELL
Partner
mick.campbell@bdo.co.uk

RICHARD BARNWELL
Partner
richard.barnwell@bdo.co.uk

NICOLA BALL
Director
nicola.ball@bdo.co.uk

CASS

JAMES STEELE-PERKINS
Partner
james.steele-perkins@bdo.co.uk

ACCOUNTING & CORPORATE REPORTING ADVISORY

MARK SPENCER
Partner
mark.spencer@bdo.co.uk

ACTUARIAL

GRAHAM HANDY
Partner & Head of Insurance Advisory
graham.handy@bdo.co.uk

SANTIAGO RESTREPO
Partner
santiago.restrepo@bdo.co.uk

ELINORE O'NEILL
Director
elinore.oneill@bdo.co.uk

GRAHAM CORNISH
Director
graham.cornish@bdo.co.uk

TAX

THOMAS TO
Partner & Head of Insurance Tax
thomas.to@bdo.co.uk

MICHAEL WHITESIDE
Director
michael.whiteside@bdo.co.uk

CORPORATE FINANCE

RAHOEL PATEL
Partner, Head of FS Transaction Services
rahoel.patel@bdo.co.uk

ADAM WHISTANCE
Director & Head of Insurance M&A
adam.whistance@bdo.co.uk

FORENSICS

RICHARD CAMERON-WILLIAMS
Partner
richard.cameron-williams@bdo.co.uk

OUTSOURCING

ROBERT HUTCHINGS
Director
robert.hutchings@bdo.co.uk

FOR MORE INFORMATION:

ALEX BARNES

+44 (0)7903 891 435
alex.barnes@bdo.co.uk

JOHN OWENS

+44 (0)7946 700 242
john.x.owens@bdo.co.uk

GRAHAM HANDY

+44 (0)7876 877 083
graham.handy@bdo.co.uk

www.bdo.co.uk