Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

Insurance Quarterly

SEPTEMBER 2018

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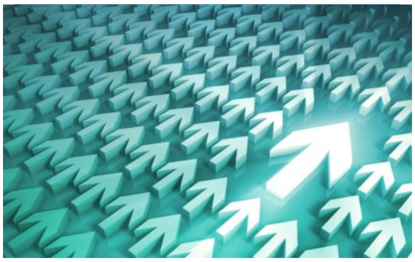

Foreword

Sylvia Cronin – Director of Insurance, Central Bank of Ireland

The changing seasons turns the focus from summer to autumn and what's left to do for the remainder of the year. Attention is also directed to speaking engagements that have taken place and those yet to be carried out. This week I had the opportunity to speak on the very important topic of cyber risk, delivering a speech entitled 'Going Digital and Remaining Safe'.

It is clear that cyber is an area of ever increasing importance, and not just to insurers. From my attendance at the EUROFI Financial Forum earlier this month, it was clear that from a banking perspective, innovation should not be carried out at the expense of consumer protection or with excessive operational risk. There must be cyber resilience throughout the whole value chain. Insurers are perhaps unique in the cyber risk arena: insurers can choose to take additional exposure to the cyber risk environment through the provision of insurance products that mitigate losses for other entities subject to cyber risk incidents. This makes awareness and understanding of cyber risk an even more crucial aspect of the operational capabilities of insurance undertakings. Supervisors also have a substantial role in ensuring the insurance sector develops a mature capability for the assessment and management of cyber risks. The World Economic Forum's 2018 Global Risks Report identified both cyber-attacks and data fraud as being in the top-five evolving risks.

From my perspective, insurers are in a unique position to help their customers improve cyber awareness and better understand and deal with cyber risks. Thus, cyber insurance providers have the potential to contribute to the management of cyber risk by promoting awareness, encouraging measurement and by providing incentives for risk reduction.

It would be my expectation that cybersecurity risks should form an integrated part of an insurer's enterprise risk management (ERM) process. It is crucial that senior management in insurance undertakings see these as organisational risks; cybersecurity transcends the IT department. One of the difficulties with cyber risks is that, unlike products and services, it's very difficult to observe best practice in other firms to compare how your firm rates. The flip side is also true, the increasing level of digitalisation has provided an opportunity for insurers to introduce new products to address cyber risks. The cyber insurance market in the EU is still at a very early stage, especially compared to the US, which is estimated to have a 90% share of the global market. GDPR is now another factor to take into the mix, and it will have an impact on the European cyber insurance sector. One of the key challenges for the European insurance sector will be to adjust to the increasing demand and changing customer needs.

From an Irish perspective, the Central Bank supervises a number of specialty insurers offering cyber risk insurance products. A particularly interesting development is the increasing popularity of insurance products to help ensure the successful management of cyber incidents. This brings new challenges for the Central Bank with an increased supervisory focus on modelling and underwriting of cyber risk insurance.

The main challenge for Regulators in designing a regulatory framework for risks associated with digitalisation is to strike the right balance between the promotion of innovation and competition on the one hand, and preserving the integrity of financial stability and guaranteeing consumer protection on the other.

Brexit continues to be to the forefront of our supervisory focus, with the outcome and timelines uncertain. The Brexit Insurance Supervisory Coordination Group continues to proactively analyse, prepare and test for the implications of Brexit. It is certain that we all face a busy few months until the end of 2018 and with the planning cycle well underway for 2019, this shows no sign of abatement. I look forward to continued engagement with you to meet the challenges ahead.

Sylvia Cronin
Director of Insurance,
Central Bank of Ireland

Risk Culture Model

Part 4 – Decision Making

In the final article in our series on risk culture, Jenny Minogue, Organisational Psychologist in the Insurance Supervision Directorate discusses decision making in risk culture. Decision making is one of the four factors of the Insurance Supervision Directorate Risk Culture Model that was introduced in the Q4 2017 edition of this newsletter.

In the Insurance Supervision Directorate Risk Culture Model 'Decision Making' is defined as: The validity and reliability of information feeding into the decision making process, the aggregation of same and the reward system in place. The definitions of the other factors and the background to the model can be found here.

Figure 1 Insurance Supervision Risk Culture Model

Decision making, it's something we do day in day out, minute by minute, consciously and unconsciously. The process of making decisions is an imperfect, complex one and seemingly routine decisions can have massive impacts on an organisation, on the economy and on people's lives. It therefore deserves our concerted attention and effort. The study of decision making is as alive now as it was in ancient Greece and to date, there has been no definitive method found that can guarantee consistent, faultless decision making. To manage expectations, the following paragraphs will not solve the mystery either, however, they will shed light on how decision making fits in to risk culture.

Risk Culture and Decision Making

In the first article in the risk culture series, I stated that although each factor of the Insurance Risk Culture model is presented in isolation, there is inevitable cross-over. Decision making was kept to the end of the series to demonstrate just that.

In order to have the best chance of making the most appropriate decisions, an organisation needs to fully understand the risks it faces. This means, having a comprehensive risk profile, accurately and reliably identifying risks and generating risk information that is balanced and presented in a salient manner. Leadership, governance and competency are all active factors that can contribute to successful decision making.

I will start with risk profile - the inventory of risks and threats an organisation is exposed to that allows it to decide what actions they are willing to take, what activities they will not engage in and what controls they need to put in place. Creating a risk profile that can form the basis of effective, sound risk management requires leaders who are capable of scanning the horizon and have the awareness to look beyond their own industry to understand what they need to prepare for and how best they can steer their organisation through on-coming threats.

Andrew Grove, co-founder of Intel Corporation, famously spoke of the paranoia he felt about all the things that could go wrong in the company. And while paranoia is not advocated here, in an effective risk culture, the leaders will be continually aware and open, they will ensure that they are speaking to the most competent, relevant experts and they will listen, even if the views are contrary to long held beliefs. Most importantly, they will be prepared to update their frame of reference to stay abreast of developments in our rapidly changing world.

When it comes to risk identification, solid governance is required to ensure it is accurate and reliable and as discussed in the article in Q1 this year, governance entails both structures and behaviours. On the one hand, there must be well developed and established procedures for detecting risks but these must be accompanied by people's action in following the procedures along with methods of reinforcing adherence to same e.g. performance management reviews. Additionally, those involved in risk identification need to possess the knowledge and skill that will allow them to perform their role to a high standard. Furthermore, decision makers need to be mindful not to dismiss identified risks due to the department or person they originate from. One tragic instance of this occurred at NASA during the Columbia disaster in 2003 in which a piece of foam detached from the shuttle on take-off, hitting against the outer layer of the shuttle resulting in the damage that caused it to disintegrate upon re-entry to the Earth's atmosphere. After the incident, staff reported that they would have spoken up about the risks of the foam strike but it would have cost them their job, that views were only welcome from particular 'castes' in the organisation and that if you were from the engineering department, you were a 'nobody'[1] . This is a cautionary tale for any organisation and should prompt decision makers to ask, what their equivalent of the engineering department is and do they consciously or unconsciously prize some views over others.

Finally, the risk information being presented to decision makers needs to be clear and unprejudiced. This is the responsibility of both the information aggregators and the decision makers. For the former, they need to steer away from data dumping and look for guidance from decision makers as to the level of information detail and context that is optimal. And from the other side, leaders need to challenge what is put in front of them to ensure they are getting the full picture and that bad news is not being filtered out. For example, dashboards can be a convenient and succinct way of presenting information however, decision makers need to be aware that aggregated data can mask harmful or potential harmful issues. Some of the ways they could challenge risk information is by querying the assumption underlying the thresholds used and requesting deep dives into particular risk areas.

Reward and Decision Making

Another aspect to consider is how decisions are rewarded. In an effective risk culture, one is not just rewarded when the outcome of a decision is advantageous or profitable but when the correct steps have also been taken throughout the decision making process. Similarly, when decisions are made that do not produce the desired outcome, even though the required procedures were followed, those who made the decision should not necessarily be punished. An organisation with an effective risk culture concentrates efforts on understanding what went wrong, asking questions like: Are we missing a step in that process? Should we have consulted more expert staff? Was this a result of an intrinsic error in our decision making process or an anomaly? Through answering such questions, the organisation can then try to modify and strengthen its decision making process.

Biases in Decision Making

Finally, no discussion on decision making is complete without making reference to the cognitive limitations and biases that negatively impact decision making. Those who have read popular texts such as 'Thinking Fast and Slow'[2] or 'Nudge'[3] , will know that biases are inherent, that we are not the rational beings theorists might like us to be and that there are innumerable cues that can lead us astray. While there are too many to highlight in detail in this article, two biases that the Central Bank of Ireland is particular concerned about are groupthink and over-confidence.

The tendency towards both is caused by natural human instinct however, to cultivate an effective risk culture, an organisation needs to firstly, acknowledge the existence of such biases and secondly, try to guard against their effects.

Thought diversity was highlighted recently by Insurance Supervisor Director, Sylvia Cronin[4] as an essential tool to try to counteract the effect of groupthink by introducing authentic challenge and alternative perspectives. Similarly, Deputy Governor, Ed Sibley[5], warns that the risk of over-confidence increases in an environment experiencing low diversity. Specifically, that over-confidence affects decision-making because the prevailing assumptions within an organisation are not subjected to internal or external challenges, and there is resistance to deviations from the status quo. So while there is no silver bullet to the cognitive limitations that can interfere with effective decision making, having a decision making group composed of those who can offer differing views, bring contrasting backgrounds and are open to challenge, is a starting point.

Conclusion

I hope the risk culture series has provided some food for thought to our readers, encouraged some reflection and indeed triggered some healthy debate. As stated at the outset, risk culture can appear to be abstract, however, I hope I have conveyed that when it is broken down into its component pieces, an informed understanding of the culture in an organisation can be established, the drivers of culture issues can be identified and changes can be made.

REFERENCES:
1) Mason, R. O. (2004). Lessons in Organizational Ethics from the Columbia Disaster: Can a Culture be Lethal?. Organizational Dynamics, 33(2), 128-142.
2) Kahneman, Daniel. (2011) Thinking, Fast and Slow. New York: Farrar, Straus and Giroux.
3) Thaler, Richard H. Sunstein, Cass R. (2008) Nudge : improving decisions about health, wealth, and happiness New Haven: Yale University Press.
4) https://www.centralbank.ie/news/article/diversity-of-thought---sylvia-cronin-director-of-insurance-supervision
5) https://www.bankingsupervision.europa.eu/press/interviews/date/2018/html/ssm.in180815.en.html

By **Jenny Minogue**,
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Countdown to EIOPA & NST Taxonomy updates

As both industry and regulators prepare for third round of annual reporting under Solvency II, it is timely to call attention to the forthcoming changes to the reporting requirements. The changes for 31 December 2018 relate to incremental corrections and amendments, with limited material changes to the reporting package.

To aid undertakings in preparing for these changes, and following the success of a similar event ahead of the 2017 year-end reporting, the Bank intends to host a reporting workshop in November 2018. Details of this event will be communicated to compliance officers in the coming weeks.

Solvency II reporting

As undertakings will be aware, the reporting requirements under Solvency II, as originally set out in Commission Implementing Regulation (EU) 2015/2450, have been amended by the European Commission in both 2016 (Commission Implementing Regulation (EU) 2016/1868) and 2017 (Commission Implementing Regulation (EU) 2017/2189).

EIOPA has proposed a number of further amendments to be applied in 2018 . While not yet formally published by the European Commission, we expect these changes to be formalised by year-end 2018 and these change have already been reflected, where necessary, in the updates to the technical implementation of the latest EIOPA taxonomy . We encourage undertakings to familiarise themselves with the proposed changes and ensure that these data are appropriately reflected in submissions from 31 December 2018 onwards.

Undertakings should also note the impending changes to the public disclosure requirements in Commission Implementing Regulation (EU) 2015/2452.

National specific templates

Since Q1 2016, the Central Bank has been receiving national specific reporting templates ("NSTs") , which address requirements specific to the local market and/or the nature of insurance undertakings supervised in Ireland and which are not catered for in the set of Solvency II harmonised reporting templates. Based on the experience from reporting to date, the Central Bank is introducing a number of amendments to the NSTs.

A summary of the forthcoming changes are set out in the table across. The required changes to the NST taxonomy to facilitate these changes will be published in October 2018, including a revised list of taxonomy validations. Our calendar on p.10 also provides key dates for external testing.

Template	Main changes
NST.01	Increased granularity of reporting of motor business (commercial vs private) Increased granularity of information of opening and closing technical provisions (reported vs. not reported) Introduction of reporting by country of risk
NST.02	Additional information on lapse rates, new business value and policy counts
NST.06	Additional information on aggregate figures (gross earned premium, earned policy count, claims provisions)
NST.14	This is a **new template**, applicable to all direct non-life insurance undertakings. The initial date of collection will be specified in due course, but is expected to be within the life cycle of this taxonomy version. This template will collect aggregate information on the number of contracts written, for each type of policy, for the main countries in which the firm operates.

IFRS 17 -
CBI Readiness Questionnaire

IFRS 17 is the new standard for insurance contracts, which will replace the existing standard, IFRS 4. The implementation date for the new standard is 1 January 2021 however firms will be required to show their accounts from 1 January 2020 for comparative purposes.

It is widely acknowledged that IFRS 17 will affect not only the financial statements, but will have a significant impact on data feeds, systems and processes within companies. The new standard will require greater levels of cross-functional interaction in the areas of finance, actuarial, I.T. and operations

IFRS 17 Questionnaire

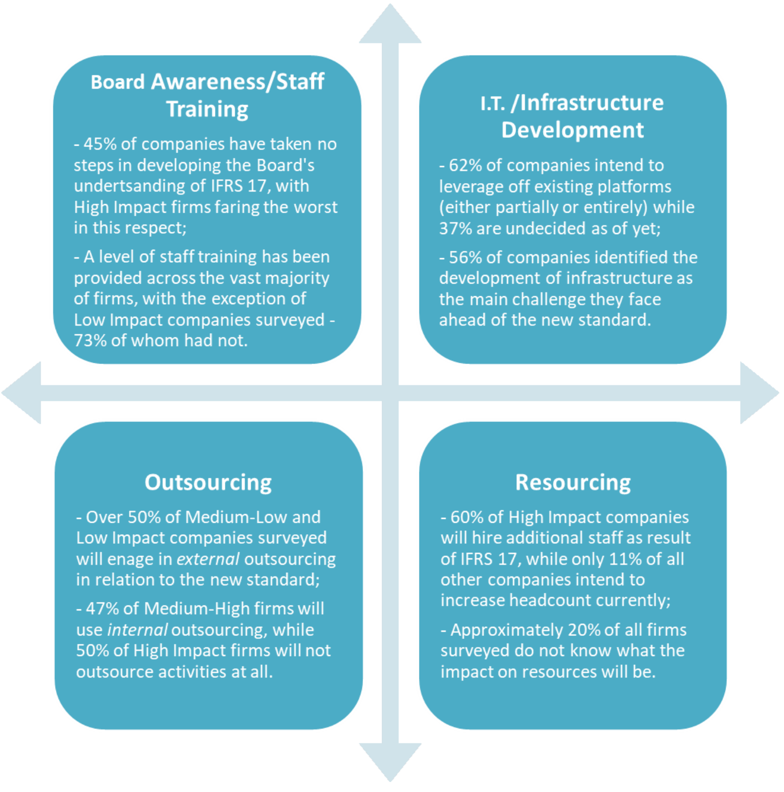
In order to gauge companies' preparedness ahead of implementation, the CBI issued a questionnaire to all IFRS Compliant High , Medium-High and Medium-Low Impact companies . A sample of Low Impact firms were also included. The survey was designed to identify the potential risks facing entities from an operational and governance perspective.

The questionnaire comprised of the following six sections:

1. Current Reporting Arrangements;
2. Governance Arrangements;
3. Preparation to date;
4. IT Infrastructure & Calculations;
5. Staff & Budgetary Constraints; and
6. Other.

Results

Results of the questionnaire offered valuable insights into the planning activities currently being undertaken by companies, as well as providing useful peer comparisons in terms of approaches selected and challenges identified. Responses were collated in groups according to their CBI PRISM Impact Rating. A summary of the key findings can be found across.



Conclusion

Companies should continue to work towards finalising their implementation plans, ensuring that the scale of changes required and the associated operational complexity is understood. From an operational perspective firms should focus on the above key areas in preparing for the standard, as well as considering the overall budgetary and strategic implications IFRS 17 will have.

The Central Bank of Ireland will monitor the operational risk exposure associated with the implementation of IFRS 17 through its on-going supervisory activities. Companies are encouraged to ensure that appropriate planning arrangements and governance structures are in in place to mitigate this risk and facilitate a smooth transition.

By **Marie Gleeson**,
Insurance Supervisor,
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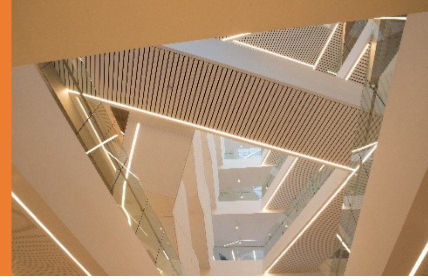
Central Bank Updates



Guidance on Fit and Proper Notification Process

On 25 July, the Central Bank published 'Guidance on Fit and Proper Notification Process for Insurance Holding Companies and Mixed Financial Holding Companies under Solvency II' (the Guidance).

The Guidance sets out further details on the Central Bank's expectations with regards to the Solvency II fit and proper (F&P) notification requirements for the roles covered in the European Union (Insurance and Reinsurance) Regulations, 2015 (the Solvency II Regulations), along with the content, form and timing of these notifications.

Regulation 261 of the Solvency II Regulations states that insurance holding companies and mixed financial holding companies (holding companies) shall ensure that all persons who effectively run the holding company must be fit and proper to perform their duties. These individuals are listed in Section 3.3 of the Guidance. In addition, the Solvency II Regulations require that holding companies must provide the Central Bank with sufficient information to enable it to assess whether the person who is subject to notification by the holding company is fit and proper to perform their duties. As such, the formal notification should take the form of a completed Individual Questionnaire sent to the relevant supervisory team in the Central Bank.

The Guidance together with the questionnaire can be found here on our website.

EIOPA Updates

EIOPA Survey on Sustainable Finance

In May 2018, the European Commission (Commission) adopted a package of measures on sustainable finance. This included proposals aimed at establishing a unified EU classification system of sustainable economic activities ('taxonomy'), improving disclosure relating to sustainable investments and sustainability risks and creating a new category of benchmarks which will help investors compare the carbon footprint of their investments. Arising from this, the Commission issued a call for advice to EIOPA in July seeking technical advice on the initial package and seeking advice on the potential integration of sustainability risks and factors into the Delegated Acts under Solvency II.

Given that this topic is at such an early stage of development, EIOPA is keen to involve market participants and other stakeholders in this work in order to obtain evidence of what is happening in practice today and facilitate the development of robust policy recommendations to Commission. These recommendations will be consulted on prior to responding to Commission. To that end, EIOPA has developed a survey for industry and representative bodies to participate in. Participation in this survey is not obligatory but would be beneficial to inform EIOPA's work on this topic. It is also an opportunity to potentially influence the thinking and direction of this work at this early stage of development.

The closing date for the survey is 3rd October 2018 and the survey can be accessed here on EIOPA's website.

EIOPA Updates

Disclosure of information to customers about the impact of Brexit

In June, EIOPA published an Opinion calling on regulators to remind insurers of their duty to inform customers about the impact of the withdrawal of the United Kingdom from the European Union. Regulators are required to ensure that insurance undertakings and insurance intermediaries take appropriate contingency measures to ensure the continuity of services for cross-border insurance contracts between the UK and other Member States of the EU. Customers and beneficiaries should be made aware of the implications of these measures both for existing and for new contracts concluded before the withdrawal date

Discussion paper on national Insurance Guarantee schemes

In July, EIOPA published a Discussion paper on resolution funding and national Insurance Guarantee Schemes (IGSs). This was a follow-up to the EIOPA Opinion on the harmonisation of recovery and resolution frameworks for (re)insurers across the Member States which was published in 2017.

EIOPA propose a harmonised approach to IGSs where the current landscape is significantly fragmented, with the existing schemes differing quite substantially in terms of financing, functions, mandate and coverage. In the discussion paper, EIOPA analysed the need for potential harmonisation of IGSs. EIOPA are accepting comments on this paper until 26 October 2018.

Links to Recent EIOPA Publications

31 July 2018	EIOPA published the third paper of a series on systemic risk and macroprudential policy in the insurance sector entitled "'Solvency II tools with macroprudential impact"
18 July 2018	EIOPA published a Q&A on Solvency II regulations. This addresses the risk-free interest rate and asset look-through.
17 July 2018	EIOPA published a report on failures and near misses in the insurance industry. This report outlines the causes of any failures and addresses early identification, to enhance insurers' understanding of such risks.
11 July 2018	EIOPA published its first Q&A on the application of the Insurance Distribution Directive. The Q&A addresses the requirements for the Product Oversight and Governance arrangements and additional regulatory requirements for Insurance-based Investment Products.
21 June 2018	EIOPA issued the latest quarterly insurance statistics. These cover the figures reported in the quarterly QRTs at Q4 2017 for insurers subject to Solvency II.

Publications & Forward Planner

Upcoming Dates

Sep

September 13th
Speech at AZN Conference –
S. Cronin

September 20th
Moderator at RBS event in Tirana –
J. Fitzgerald

Oct

**October 18th
Publication of NSTs v1.3**

October 24th
Speech at Insurance Ireland forum –
D. Rowland

October 25th
CBI & Trinity College Panel on Culture & Diversity – S. Cronin

Nov

**November 2nd – 8th
External UAT: EIOPA Taxonomy 2.3**

November 6th
Speech at IDA Jurisdictional Insights Event –
S. Cronin

Dec

December 4th
Panellist at Insurance Risk & Capital Conference – S. Cronin

**December 7th – 12th
External UAT: NSTs v1.3**

Recently Published

Date	Publication/Communication	Link
27 July 2018	'A well-functioning financial system is necessary to meet long-term challenges including raising living standards' – Speech by Governor Philip R. Lane	https://www.centralbank.ie/news/article/PRLMacGill26July2018
12 September 2018	'The Banking Crisis – A Decade On' – Speech by Ed Sibley, Deputy Governor – Financial Regulation	https://www.centralbank.ie/news/article/the-banking-crisis-a-decade-on-ES12Sept2018
13 September 2018	'Going Digital and Remaining Safe' – Speech by Sylvia Cronin, Director of Insurance Supervision	https://www.centralbank.ie/news/article/'going-digital-and-remaining-safe'-sylvia-cronin

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