Banc Ceannais na hÉireann
Central Bank of Ireland
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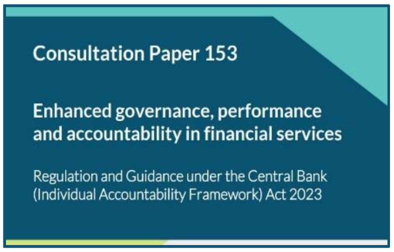
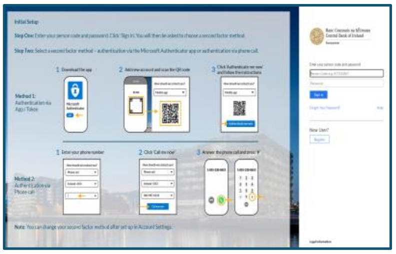
Insurance Newsletter

MARCH 2023


Consultation Paper 153

Enhanced governance, performance and accountability in financial services

Regulation and Guidance under the Central Bank (Individual Accountability Framework) Act 2023



Insurance Insights

General Insurance Pricing Discipline

The changing environment with evolving claim trends, persistent inflationary pressures and shifting consumer behaviour with a challenging economic outline requires strong pricing discipline. This includes robust oversight of pricing, close monitoring of rate adequacy, pricing assumptions, policyholder behaviour and changes in the risk profile of business underwritten.

Robust pricing frameworks provide management with the control to steer firms through uncertain times. Robust frameworks will support sustainable business models, ensure risks are understood and that appropriate action will be taken. Central to pricing decisions, the frameworks must bring customers front of mind, ensuring the impact of pricing practices on customers and ensure fair outcomes are central to decision making.

Some better practices we have observed when refining frameworks to enhance pricing governance, reporting and oversight of emerging risks are set out within this article.

General Board Oversight of Business Lines

The priority and focus on pricing discipline starts in the Board room. Board oversight of pricing can be supported by setting a well-defined firm-specific underwriting risk appetite, with targets for monitoring and clear ownership of rate adequacy at Board level. Some good practice observed in this regard includes:

- Regular pricing-specific updates provided to the Board with clear indicators of where growth is relative to the previous year, the plan, or risk tolerance e.g. GWP exceeds plan by 10% = amber rating.
- Risk management frameworks contains clearly defined actions should a breach occur where profitability or growth is outside of risk appetite.
- Ensuring a fully embedded consumer protection risk management frameworks are in place to drive positive consumer focused culture.
- Oversight & Commentary and analysis e.g. discussion on rating environment, competitor behaviour, consumer demand and consumer impact.
- Training to ensure robust oversight of pricing processes, for example new pricing techniques or the use of big data and related technologies within pricing processes.
- Where there is reliance on the group business plan, Boards scrutinise and challenge to ensure it is appropriate for the firm.

Dynamic Pricing Reporting

Dynamic and timely pricing controls will evaluate technical prices and project rate adequacy to deliver sustainable profits while also prompting action needed to manage risks arising for consumers. Observed good practice includes:

- Comprehensive pricing reports showing pricing dynamics by lines of business. This includes transparency of trends in profitability, rate changes versus growth, complimented by how much of the growth is rate increase or volume growth.
- Pricing models recalibrated regularly with feedback loops from other area of the business (e.g. reserving, finance, operations, sales, underwriting and claims).
- Standard reporting metrics by line of business (e.g. premium levels, exposure, price adequacy and rate changes) complimented by additional monitoring of growth areas. For example, more granular

analysis of lines of business (e.g. key contracts, by broker, distribution channel, territory, industry).
- Explicit consideration of anti-selection. For example, through monitoring business mix trends, or by tracking bound as a proportion of quoted.
- Ability to track pricing implementation against targets e.g. proportion of risks that have been through a pricing model, deviations from the technical price.

"As pricing models are being refined and developed, transparency is critical. Firms should consider broader implications including Board oversight, the impacts on consumers and transparent reporting of profitability."

Transparency of Current and Emerging Risks within Firms

Pricing frameworks that identify, assess and report on current and emerging risks are the foundations of good pricing discipline. Consumer considerations should be central to consideration of current and emerging risks. Boards should consider expectations[1] of firms in relation to the risks arising for consumers from the more challenging economic outlook in particular. Firms should be analysing trends and have processes in place for those most vulnerable to the current economic environment. The recent EIOPA statement on inflation, published in December 2022, sets out some supervisory expectations in this regard. Good practices observed include:

- Transparency regarding the allowance made within pricing for various changing trends is critical to avoid opaque or unclear assumptions.
- Relevant emerging trends impacting the firm should be identified and the pricing impact communicated, such as the evolving economic outlook; changing court awards, explicit allowance for current and future inflationary pressures including the impact of inflation on various claim types; changes in the cost and availability of reinsurance.
- Articulation of how pricing models are evolving and ensuring transparency of related risks. Examples include risks relating to new pricing techniques or the use of big data.
- Pricing risks integrated into risk management frameworks and ORSA processes, including consideration of the combined impact of various risks or scenarios.
- Transparency regarding the use of external data to validate assumptions or indeed to supplement internal data where own data is not sufficiently credible.
- The allowance for climate change in underwriting and pricing varies significantly across the market. In general, firms are focusing on managing the impacts of physical risks (e.g. increased forest fires or flooding), managing the firm's own policies and reputational risk; and managing the firm's own contributions to net-zero targets. Good practice also includes addressing the impact of transition risks on the business model and potential litigation e.g. due to errors and omissions in climate change reporting.

Conclusion

The current Irish general insurance environment exposes firms to various emerging risks, some of which may mask or offset each other temporarily. Pricing frameworks should transparently identify and highlight risks and trends, facilitating timely action and pricing discipline. This will help ensure the general insurance market operates in the best interests of consumers and the wider economy.

Grace von Offenberg Sweeney
Head of Function - Actuarial
Insurance Supervision Directorate

1. A Dear CEO letter was issued in Q4 2022 by the Central Bank to all firms setting out actions to consider in relation to the risks arising for consumers from the more challenging economic outlook.

Insurance Insights

Supervisory Priorities

On 31 January 2023, Insurance ERM published an interview with Domhnall Cullinan, Director of Insurance Supervision. The interview covered a range of topics including Brexit, Solvency II, Climate Risk, Sustainability and Diversity. Below we highlight Domhnall's remarks on our insurance supervision priorities across 2023, and on current risks facing the insurance sector. The full interview can be accessed here on the Insurance ERM website.

Domhnall on Insurance Supervision Priorities:

Individual Accountability – "The Central Bank Individual Accountability Framework Bill is currently before Ireland's parliament, and we anticipate the bill will come into force early this year (*see Page 5 for update*). We will then go to consultation in relation to various standards and guidance. The ruling will have serious implications for insurers. It will make it easier for the Bank to pursue individuals and make them more accountable. The intention is not that it will lead to any huge uptick in enforcement, but it may change the nature of it. In the past, our emphasis was pursuing firms because the Bank had to sanction the firm first before you could pursue the individual. But now the Bank can pursue individuals within firms."

Climate Change – "In 2022, the Central Bank developed a heat map for climate risk within insurers and we will be using that to focus our efforts on the firms in 2023 that we view as having the highest climate exposure. A second big pillar of our climate related work in 2023 in relation to this is we have a natural catastrophe project that is going to focus on whether the NatCat modelling is adequate overall, whether it is properly modelled for Irish specific risks, and whether NatCat modelling takes climate risk into account."

Consumer Interest – "The Central Bank undertook a lot of work on value for money in unit-linked products last year and we will build on that this year to see if there are any outliers in terms of charging. We will also be undertaking a thematic review on the EIOPA Supervisory Warning on Credit Protection Insurance."

Operational Resilience – "This is a topical area and is one of the areas I am concerned about in 2023. The Central Bank has issued cross-industry guidance on operational resilience which will come into force fully by the end of this year. And then the [EU's] Digital Operational Resilience Act should come into effect around the end of 2024."

Domhnall on risks facing insurers in 2023:

Inflation – "I have seen commentary in the media that inflation has peaked but even if this turns out to be the case, it certainly has not gone away, and we still say to insurers you have to be mindful of the impact of inflation on costs, claims, operating expenses and allowances made for reserving in existing business."

Market volatility – "This remains a big issue. We saw what happened with the UK gilts crisis and with Covid-19, Russian invading Ukraine and Brexit; you would have to question the market's ability to absorb further surprises in an already high-risk environment.

Cyber Risk – "the one thing I would be concerned about, from an Irish perspective, is that the Irish insurance industry doesn't find itself as large provider of capacity in the international market, but without appropriate pricing and adequate reserving and the right expertise to underwrite the risk."

Readers are also reminded that in February 2023, Sharon Donnery (Deputy Governor, Financial Regulation) and Derville Rowland (Deputy Governor, Consumer and Investor Protection) wrote to the CEOs of all regulated firms. Their letter sets out the Central Bank's key regulation and supervision priorities for 2023, and their views on the operating environment. The letter can be viewed here on the Central Bank of Ireland website.

Central Bank Individual Accountability Framework (Act 2023)

On the 9 March 2023, President Higgins formally signed the Central Bank (Individual Accountability Framework) [IAF] Bill into Irish Law enacting what is now the Central Bank (Individual Accountability Framework) Act 2023. This is the culmination of a significant amount of work within the Central Bank working closely with the Department of Finance over the past number of years to bring these proposals to fruition.

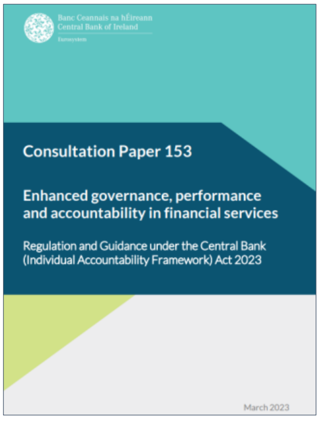
The key areas covered by the legislation are:

1. A **Senior Executive Accountability Regime** (SEAR) which ensures clearer accountability by imposing obligations on in-scope firms and senior individuals within them to set out clearly where responsibility and decision-making lies for their business;
2. **Conduct Standards** which set out the standards of behaviour the Central Bank expects of firms and the individuals working within them;
3. **Business Standards**. The legislation provides for the Central Bank to set out standards to be met by businesses, not just individuals. (Currently such standards are set out in the Consumer Protection Code. They are being reviewed as part of the current review of the Code and therefore will not be consulted on as part of the IAF consultation).
4. **Enhancements to the current Fitness & Probity (F&P) Regime** to take into account certain modifications of the existing F&P Regime; and
5. **Enhancements to our Administrative Sanctions Procedure**, including a key change regarding the Central Bank's ability to take enforcement directly against individuals for breaches of their obligations rather than only for their participation in breaches committed by a firm.

Impact for the insurance sector

All firms need to be effectively managed and organised, individuals need to be clear what they are responsible for, and both need to be accountable if they fall short of expected standards. It is essential to be clear on roles and responsibilities in firms, particularly large and complex institutions where things can and do go wrong through systems error and individual conduct.

All aspects of the IAF will apply to insurance undertakings (excluding SEAR), therefore all insurance undertakings will be required to adhere to the new framework. The SEAR will apply to "in-scope firms" (i.e. all insurance undertakings including third country branches but excluding reinsurance undertakings, captives and SPVs).



The consultation also includes a proposal to introduce a new PCF-50 Head of Material Business Line Business for insurance undertakings. This follows the introduction of the PCF-50 for credit institutions in October 2020. The Head of Material Business Line for insurance, is an individual who has significant influence over the performance of a material line e.g. oversees the performance of that business line and the business line in question satisfies certain quantitative criteria. (Please refer to the consultation paper for more detail).

Implementation

While the key components of the IAF have been communicated for some time, it is acknowledged that firms and holding companies will need time to prepare for and implement the various elements of the IAF. The following implementation timeline is proposed:

- Conduct Standards including accountability of senior individuals for running their parts of the business effectively to apply from 31 December 2023;

- Fitness & Probity Regime – Certification and inclusion of Holding Companies to apply from 31 December 2023;
- Regulations prescribing responsibilities of different roles and requirements on firms to clearly set out allocation of those responsibilities and decision making to apply to in-scope firms from 1 July 2024.

Consultation

The Central Bank have issued Consultation Paper 153 on the IAF. The consultation is open for 3 months from 13 March to the 13 June 2023. Feedback is invited from interested parties on the consultation paper. It is the policy of the Central Bank to publish all responses to its consultations on our website. A separate consultation process will take place on the Administrative Sanctions Procedure element of the IAF in late Q2 2023. Please submit any comments/feedback on the IAF to IAFconsultation@centralbank.ie

Anne-Marie Butler,
Senior Lawyer,
Advisory Team,
Insurance Supervision Directorate

AXA Life Europe DAC

On 8 December 2022, the Bank reprimanded and fined AXA Life Europe DAC (ALE) €3,640,000 in respect of three breaches under the European Communities (Life Assurance) Framework Regulations 1994 (S.I. No. 360 of 1994) (1994 Framework Regulations), the Corporate Governance Requirements, and the Solvency II Commission Delegated Regulation (EU) 2015/35 (Solvency II Delegated Regulation).

The breaches:

- ALE failed to put in place an effective process to identify, manage, monitor and report the risks arising from a cohort of policies, for which terms and conditions were not clear.
- ALE failed to establish effective conflict of interest policies and procedures and failed to conduct an adequate assessment of potential conflicts of interests

The fine – the Bank determined the appropriate fine to be €5,200,000, which has been reduced by 30% to €3,640,000 in accordance with the early settlement discount scheme provided for in the Central Bank's Administrative Sanctions Procedure.

Key messages:

- It is important that firms identify, assess and manage the risks to which they are or might be exposed, to ensure that they can meet their commitments to consumers. Weak internal controls will result in failures to appropriately monitor these risks.
- Firms must also manage conflicts of interest appropriately and establish and apply robust mechanisms for doing so. Conflicts of interest are an inherent risk to all regulated entities and, when not properly managed, they pose a risk to consumers and diminish market integrity.
- The sound supervision of cross-border activities, be it under free provision of services or the right of establishment, is an important part of the Central Bank's mandate. This case demonstrates the effectiveness of close collaboration between the Central Bank and other financial regulators across the EU, in enhancing financial stability and the protection of consumers.

Outsourcing Register

Further to the Central Bank's communication in the Guidance Notes accompanying the Outsourcing Register Templates in August 2022, noting a submission date of February 2023 for the year-end 2022 register. Please be advised that the submission date has been deferred to Q4 2023. The Central Bank intends to publish the template for this submission in Q2 2023 and will advise a specific submission date in due course.

Insurance Updates

Insurance Directorate - Recent Stakeholder Engagement

Under the "Open & Engaged" theme of our organisational strategy, the Central Bank of Ireland undertakes regular speaking engagements, providing an opportunity to engage with our stakeholders, to outline forthcoming regulatory developments and supervisory plans, to highlight emerging risks, and to summarise the key findings and required actions arising from recent review work. A summary of stakeholder engagements from Q1 2023 is provided below.

On 10 March 2023, Domhnall Cullinan, Director of Insurance Supervision, spoke at the launch of the Insurance Industry ESG Knowledge and Skills Analysis Report. Domhnall welcomed the publication of the report, remarking *"It is increasingly the case that developing a clear understanding of Environmental Social and Governance considerations and embedding these within corporate strategy will play a vital role in delivering value to all stakeholders. The publication of the ESG Skills Report is an important milestone for the insurance industry on this journey."* Domhnall also took the opportunity to reiterate insurance supervision priorities for 2023.

(Domhnall Cullinan (second from left) at the launch of the ESG Knowledge and Skills Analysis Report 2023)

Forthcoming Information Requests

As supervisory engagements are progressed, information requests will be made of some (re)insurers in the coming weeks, including:

- A questionnaire will issue to selected non-life (re)insurance undertakings, as part of an examination of how Natural Catastrophe risks are being modelled and managed, including how modelling is being adapted and revised to take climate change risks into account.

- Information requests may also be issued to firms within scope of planned thematic inspections, for example in relation to a 'deep dive' on operation resilience frameworks.

- In relation to consumer protection, requests for information will be issued in support of a planned assessment of firms Risk Management Frameworks and in relation to the Differential Pricing Regulations.

The Central Bank would also like to acknowledge the participation of a number of (re)insurance undertakings in the digitalisation survey launched in Q4 2022 – for which there was a response rate of greater than 95%. The results of the survey are being collated and analysed, and will inform further supervisory work in this field. Key observations will be published in early Q2.

EIOPA Statement on Governance in Third Country Branches

On 3 February 2023 EIOPA published a Supervisory Statement which is intended to strengthen the supervision and monitoring of insurance undertakings' and intermediaries' activities when using governance arrangements in third countries. Given that such governance arrangements may lead to poor risk management, ineffective decision-making and pose operational, reputational, and financial risks – also to policyholders – EIOPA has decided to clarify its supervisory expectations. EIOPA and the Central Bank will closely monitor market developments regarding the use of third country governance arrangements following the publication of the Supervisory Statement.

Sustainable Insurance

CP 151 – Guidance on Climate Change Risk

The Central Bank's consultation on Guidance for (Re)Insurance Undertakings on Climate Change Risk (CP151) closed in October 2022. We have received four formal responses to the consultation and we intend to publish the Feedback Statement to the consultation, and the Final Guidance, on 27 March 2023. The Bank will further engage with industry post-publication to support the understanding and implementation of the Guidance.

Recent EIOPA publications related to sustainability.

In recent months EIOPA has published a number of sustainability related papers. On 5 December 2022, EIOPA published a Discussion Paper "Prudential Treatment of Sustainability Risks" which set out the intended scope, methodologies and data sources for EIOPA's risk based analysis to address the influence of sustainability risks underlying investment and underwriting activities. The discussion paper also considered the prudential treatment of social objectives and risks under Solvency II. The consultation closed on 5 March 2023.

On 26 January 2023, EIOPA published its Opinion on the European Financial Reporting Advisory Group's technical advice concerning European Sustainability Reporting Standards (ESRS). The European Sustainability Reporting Standards, once final and adopted, will set out what sustainability-related information firms falling under the scope of the Corporate Sustainability Reporting Directive (CSRD) will be required to report. The CSRD will apply, progressively, as of 2024 and will require all large and listed companies (except micro-companies) to disclose information on the environmental, social and governance risks that their business is exposed to and on how their business impacts people and the environment.

On 6 February 2023, EIOPA published its Report on insurers' inclusion of adaptation measures to climate change in their non-life underwriting practices. It reports on the outcome of a pilot exercise which EIOPA conducted during 2022. The report notes that only 23% of total losses caused by extreme weather are currently covered by insurance and describes a number of adaptation measures that could reduce the risk.

Additionally, EIOPA has issued a Call for Evidence regarding the re-calibration of the NatCat Standard Formula parameters. The Call for Evidence has been issued to regulators, insurance and actuarial associations and the NatCat Expert Network Group and seeks to identify which elements need recalibration and if any new perils should be added. Responses are due by the 30 March 2023.

Sustainable Finance Disclosure Regulation (SFDR)

On 17 February 2023, an amendment to the Sustainable Finance Disclosure Regulation (SFDR) regulatory technical standards (RTS) was published in the Official Journal (OJ).

The impact of the amendment is to amend the information to be included in pre-contractual disclosures, websites and periodic reports so that the exposure of financial products to investments in fossil gas and nuclear energy activities is now included in the disclosures. It also introduced some minor amendments to the SFDR RTS. The amended SFDR RTS took effect on 20 February 2023.

Central Bank Updates

Publication of Consumer Protection Outlook Report

[The Consumer Protection Outlook Report 2023](#) outlines the five key drivers of risk for consumer of financial services in Ireland and our expectations on how firms should manage these risks to avoid consumer harm.

These risk drivers reflect the feedback and engagement from our key stakeholders over the last year, following our request to hear people's views on the risks in our 2022 Outlook Report. This feedback was incorporated into our annual risk assessment, which has confirmed anchoring on five Key Drivers of Consumer Risk:

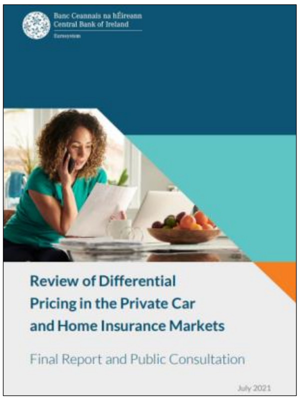
- The changing operational landscape;
- Poor business practices and weak business processes;
- Ineffective disclosures to consumers;
- Technology-driven risks consumer protection; and
- The impact of shifting business models.

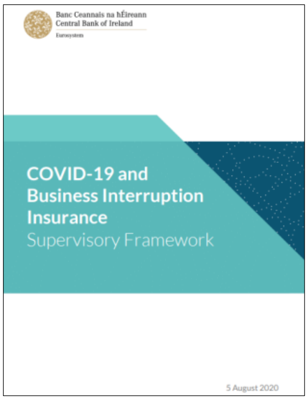
Director of Consumer Protection, Colm Kincaid, has stated: *"By anchoring on these risk drivers for our work in 2023 and beyond, we hope to also provide a degree of predictability and certainty for regulated firms. This will mean regulated firms can similarly devote their efforts to making long-term sustainable improvements under these headings. We believe sustained concrete action by the firms we regulate on these Key Drivers of Consumer Risk would make a material positive difference for consumers of financial services. For our part, we will continue to set high expectations of the firms we regulate and scrutinise how they meet those expectations."*

Planned Review of Firms' Risk Management Frameworks

As outlined in the Outlook Report, the fundamental responsibility of a financial service provider is to provide a good quality service in a manner that places the best interests of the consumer at the centre of how that service is designed and delivered.

Poor business practices and weak business processes disrupt this, and can lead to consumer harm. Where firms do not have adequate processes and procedures to control and mitigate operational risks, this can have a severe impact on the quality and availability of the service provided to consumers. An absence of consumer-focused culture aggravates this risk, making it imperative that regulated financial service providers adopt a consumer-centric approach to how they develop their businesses practices and processes. As set out in the Outlook Report, we will engage with firms where we identify weaknesses in consumer-focused culture with a view to firms taking concrete action to remedy the situation.





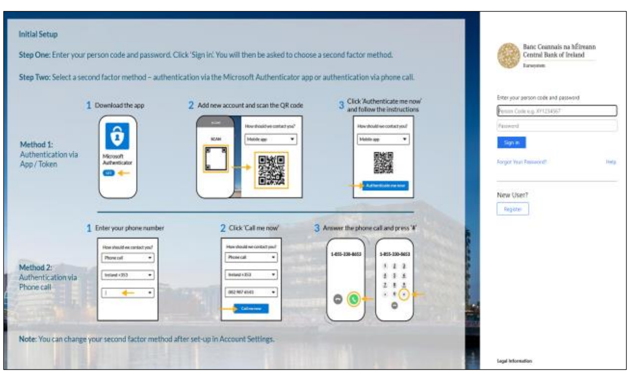
While absence of consumer-focused culture is a key cross-sector risk, we have seen instances in the insurance sector where we believe ineffective internal oversight and controls have resulted in decision making that has fallen below the standards and the consumer-centric approach expected by the Central Bank. Evidence of such weaknesses were identified in the insurance sector specifically through the work we completed in relation to differential pricing in the motor and home insurance markets and the examination completed in relation to business interruption insurance from the outset of COVID-19 and its impact on certain businesses. In order to ensure more effective and efficient business practices and processes within firms, they need to be underpinned by a more embedded consumer-focused culture at senior management level to assist in the identification of consumer risks and incorporation of consumers best interests in decision-making.

Central Bank Updates

The Central Bank has decided to undertake a review focused on this area. The review aims to assess the appropriateness of insurance firms' risk management frameworks and in particular how they manage and mitigate the risks posed to consumers. It will align with our [Consumer Protection Risk Assessment](#) (CPRA) model and will be completed across the insurance market. The CPRA will include a desk-based review of certain firms' processes and procedures, including control functions, consumer monitoring and reporting and risk identification and management, followed by on-site walkthroughs and interviews to understand firms' framework design and effectiveness. This review will run throughout 2023; we will engage with in-scope firms in the coming weeks and months.

New Fitness & Probity Application Process

Our systems are being enhanced to facilitate the submission of applications to become a holder of a Pre-Approval Controlled function (PCF). Individual Questionnaires (IQs) will no longer be submitted via the Online Reporting System (ONR), but will instead be submitted via the [Central Bank of Ireland Portal.](#)



(*Landing Page for the Central Bank of Ireland Portal*)

These changes are planned to become operational on 24 April 2023, and will provide applicants with an enhanced process for submitting applications. A new IQ has been developed and must be used for PCF applications submitted from 24 April 2023. We plan to publish the new IQ on 30 March. The new process for submitting IQs consists of 3 parts which are described hereafter:

(1) Account Settings

First, the applicant registers as a Portal User and enters the user's name and address on the system. The point of contact and the proposer must also register as Portal Users.

(2) F&P Profile

Second, the applicant creates their F&P Profile which contains information that would typically be in a Curriculum Vitae. It must be entered before completing step 3 below; and is retained on the system so that it can be updated and re-used for subsequent PCF applications.

(3) PCF Application

Finally, the applicant and proposer complete this part of the IQ which is similar to the existing application form. The main difference is that information that the applicant has already entered in the F&P profile is pre-populated into PCF Application. The preliminary questions are divided between the proposer and the applicant. The application form is then tailored to the applicant based on these answers. Supporting documentation may be uploaded.

Once all 3 sections have been completed, the proposer submits the application to the Bank for assessment. Any communication with the F&P team regarding the PCF application will be via portal messaging and not by email. If the application needs to be amended, the unlock process has been simplified. In addition, the status of the application can be tracked on the Portal. For example if an IQ is on hold, the reason why will be displayed.

Further information on the new system has been published [here](#).

Potential Action Required

If you are a proposer or applicant, and not already registered as a Portal user, you can register now. Guidance on how to do so is located [here](#) on the Central Bank website.

Forward Planner

Upcoming Dates

Mar — Apr — May — June

24 April 2023 – CBI Portal opens for F&P IQ Applications

8 April 2023 – Submission Deadline for Solvency II Solo Annual Returns

13 June 2023 – Closing date for CP153 (Individual Accountability Framework)

Central Bank of Ireland – Speeches/Public Consultations

Date	Topic	Link
13 March 2023	Launch of public consultation on key aspects of the implementation of the Individual Accountability Framework (IAF), including the publication of draft regulations and guidance.	https://www.centralbank.ie/publication/consultation-papers/consultation-paper-detail/cp153-enhanced-governance-performance-and-accountability-in-financial-services-regulation-and-guidance-under-the-central-bank
10 March 2023	"The importance of enhanced diversity and inclusion within the financial services sector" - Remarks by Deputy Governor, Derville Rowland at Walkers Ireland	https://www.centralbank.ie/news/article/diversity-and-inclusion-within-the-financial-services-sector-remarks-by-deputy-governor-derville-rowland-at-walkers-ireland

Contact Us

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