CLIFFORD CHANCE

INSURANCE GLOBAL 2017

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INSURANCE GLOBAL 2017

Welcome to our Insurance Global publication which outlines global legal developments in the insurance sector in 2017. This edition highlights developments on the global stage with legal updates from China, Germany, Italy, Luxembourg, Spain, the UAE, the UK and the US.

Increased conduct regulation (for example, the Insurance Distribution Directive ("**IDD**") in Europe), Insurtech innovation, cybersecurity and data privacy are themes that have dominated the global insurance market over the past 12 months. Our lawyers have pinpointed these as significant areas of focus in their practice as the insurance market looks at new ways to reach customers and use key data to benefit their customers and their businesses.

The heightened focus on insurers' governance is another trend spurred on by increased financial and regulatory reporting requirements with many of our insurer clients responding by adjusting their internal operations and corporate strategies. Restructuring and reorganisations are also driven by political events, in particular Brexit (with many insurers establishing a presence in the EEA and UK to enable them to continue to operate in a post Brexit world) and as always, market events including significant mergers and acquisitions continue as a response to regulatory change such as Solvency II. The soft insurance market has continued to impact insurers and reinsurers and ongoing low interest rates are creating pressure on their investment returns. Their response has been to look for new areas of risk and geographic coverage, to measure investment in alternative assets in an attempt to improve returns on existing operations, to streamline their operations and seek maximum capital efficiency.

Recent natural catastrophes in America and the Caribbean may lead to some hardening in certain sectors of the insurance market. The 2017 hurricane season has tested the resolve of some existing market participants in Insurance Linked Securities ("**ILS**"). Despite this, ILS is still expected to attract increased investment from capital markets investors. Both the UK and Singapore are seeking to establish new centres for ILS issuance. Bermuda has also continued to see interest in the establishment of further 'hedge fund Re' specialist reinsurers, which are also providing additional capacity in the reinsurance market.

Global M&A activity has continued but with fewer major mergers this year. Asia has been an active market and both Chinese and Japanese insurers have been active abroad, however Chinese buyers have recently found regulatory approvals more challenging in some markets, notably the USA. In Europe we continue to see disposals of non-core or capital intensive businesses post-Solvency II, with private equity and run off specialists as active buyers.

We expect further regulatory changes in 2018 as regulators continue to respond to market and legal developments affecting the insurance sector. In 2018 Brexit planning and responding to Brexit developments will no doubt continue to be a focus for UK and EU based insurers as they hopefully get more clarify on post Brexit access arrangements, we also expect to see regulators refocusing on the prudential regulation of insurers. For example, the European Commission, as well as some National Competent Authorities, will start to look at the implementation of Solvency II across Europe for example, in respect of and improvements to the Matching Adjustment[1]. At the same time and at a global level, the International Associations of Insurance Supervisors ("**IAIS**") is looking at the phased adoption of Insurance Capital Standards ("**ICS**") for Internationally Active Insurance Groups and an Activity Board Approach for assessing the systematic risk of insurers. Conduct regulation will continue to be a focus and challenge for regulators globally as will cybersecurity and Insurtech, with global regulators recognising the need to understand the impact of technology on insurers' business and operations and whether current regulatory principles cover new processes and new products adequately. We also expect increased convergence of global regulation but also some tensions in establishing such an approach to regulation, for example, some countries are actively attempting to open some of the insurance market to overseas participants but this is contrasted by increased local protection of business in some areas given political trends in some part of the world.

We hope that you enjoy reading this global review. If you require further information on any particular topic referred to or more generally, please do not hesitate to get in touch – our specialist global sector group can support our insurance clients in assessing the impact of global and local legal and regulatory trends on their businesses. Our contact details can be found at the end of this publication.

The Insurance Sector Team

1 The Matching Adjustment ("MA") are provisions within the Solvency II legislation which have the effect of cushioning certain life insurers' capital resources, subject to conditions and prior approval, when they can demonstrate that the cash flow of a designated portfolio of assets is matched to the life insurance liabilities.

1. CHINA

1.1 In recent years China has witnessed a fast growing insurance market. Two notable growth trends are: first, the liberalisation of the Chinese insurance market to specifically encourage foreign investment and, second, the rise of the Chinese health insurance market. Although these two trends are the focus of this article, one other notable development includes a White Paper on China Insurance Technology Development released in May 2017, which analysed the joint development of, and cooperation between, insurance sector and technologies, such as blockchain, artificial intelligence, the cloud and big data. Generally, Insurtech is expected to revolutionize the Chinese insurance industry by bringing disruptive products and services to a market that is fast adopting, and increasingly moving toward, an online ecosystem. The market is also seeing a surge in the number of people who are aware of and are starting to understand the benefits of insurance. The Clifford Chance Beijing, Shanghai and Hong Kong Offices are keeping abreast with the legal issues resulting from the growth of Chinese Insurtech as well as actively monitoring and advising clients on other Chinese insurance sector developments.

Foreign investment

1.2 Whilst regulations governing the insurance sector have been, in many aspects, strengthened in recent years, Chinese regulators are conscious of the importance of further liberalising China's insurance market to international players. In August 2016, the Insurance 13th Five-Year Plan (the "**Plan**") was released by the Chinese government, with one of the objectives being to improve the international competitiveness of China's insurance industry. The Plan emphasised that the insurance sector should facilitate China's Belt & Road initiative[2] and encouraged more pilot schemes being launched in free trade zones – these pilot schemes include, for example, the mutual recognition of insurance products, schemes to establish a market connection between free trade zones and Hong Kong, Macau and Taiwan and schemes to encourage insurers' participation in foreign currency long-term life insurance, cross-border Renminbi reinsurance, pension, entertainment and cultural insurance etc.. In addition, Chinese insurers are encouraged to establish, acquire or invest in overseas insurance institutions to build up their global network, while Hong Kong, Macau and Taiwan insurers are encouraged to deepen their cooperation with mainland insurers.

1.3 At various public conferences and forums, Chinese authorities and senior officials have made strong indications that China welcomes more cooperation and investment from foreign insurers. For example, in November 2016 during the 2016 UK-China 8th Economic and Financial Dialogue, China agreed to work towards lifting the foreign ownership cap on life insurance firms operating in Mainland China. In particular, the China Insurance Regulatory Commission ("**CIRC**") indicated that it would welcome and encourage qualified UK firms to apply for licenses and do business in China through wholly-owned subsidiaries

2 China's Belt and Road Initiative ("**BRI**") is the most ambitious geo-economic vision in modern times. Committing to $1 trillion in new infrastructure projects, scores of trade agreements, and countless people-to-people ties, it seems set to crown China's place on the global stage. The primary of the BRI is its overland routes between China and Europe

and joint venture companies. In addition, the Chinese authorities welcome the collaboration of Chinese (re)insurers and UK (re)insurers for providing sufficient insurance coverage for China's Belt & Road projects. In January and August 2017, the Chinese State Council echoed the call to further open up the Chinese financial service sector, reduce restrictions on foreign investment in financial institutions (which include insurance companies and insurance intermediaries) and to offer more tax incentives to investors.

1.4 Although strong indications to encourage foreign investors have been made clear by Chinese officials, detailed measures and rules are yet to be issued. It is possible that China may adopt the approach whereby the shareholding restriction on foreign investors will be gradually removed through pilot programmes in China's free trade zones, allowing wholly foreign-owned life insurers in certain specific areas.

Health insurance

1.5 One of the areas potentially open to a full foreign ownership could be health insurance. The health insurance market in China has been growing vigorously over the past few years, catching the eye of both domestic and overseas insurers. According to statistics released by the Insurance Association of China ("**IAC**"), over the past five years, the total premium of health insurance has grown from RMB86.3 billion in 2012[3] to RMB404.25 billion in 2016[4], representing an increase of 368.42%. The first eight months of 2017 have already generated a premium of RMB319.49 billion, surpassing the RMB309.82 billion of the same period of 2016. The explosive growth is largely driven by favourable policies – since September 2013, the State Council has issued a series of opinions and circulars on facilitating faster growth in commercial health insurance services, which stressed the need to enrich health insurance product types and enhance cooperation between health insurance and pension services.

1.6 So far, seven specialised health insurance companies have been incorporated in China. However, some of them are still struggling to profit in face of competition and unsatisfactory cooperation with medical institutions. While it remains to be seen what China's regulators will decide for the detailed new regulations governing health insurance business, it is currently expected that health insurance may be treated by the regulators as a standalone category of insurance business, specific regulations may be developed to address specific demands of health insurance business such as a lower minimum capital requirement than that required of other insurance businesses, and that more platforms may be created to support health insurance companies' work with medical institutions in pursuit of affordable and quality medical services.

1.7 The Chinese insurance market has too much potential to be left behind. Introducing more international business expertise, foreign capital and sophisticated market players into this sector, as the Chinese regulators currently endeavour to, will undoubtedly benefit China's insurance market in the long run.

3 Data source: http://www.iachina.cn/art/2013/1/23/art_617_11075.html.

4 Data source: http://www.iachina.cn/art/2017/2/22/art_617_94214.html.

2. FRANCE

2.1 The French insurance market is the fourth largest in the world after the US, Japan and the UK. It is also the second largest European market as measured by the amount of premiums collected, according to Insurance Europe (the European insurance and reinsurance federation) in its statistical report for the 2016 financial year, and two French groups are ranked in the 10 world's largest insurers or reinsurers. From a legal and regulatory perspective, the two last years have been very active for the French insurance market with the implementation of the European directive Solvency II in France (which entered into force on 1st January 2016), the management of the immediate consequences of the 23 June 2016 referendum vote for the UK to exit the EU ("**Brexit**"), the protection of consumers with the upcoming entry into force of the Insurance Distribution Directive ("**IDD**") that France must implement by 23 February 2018 and adapting strategy, compliance and processes to respond to the growth in Insurtech opportunities.

IDD

2.2 IDD was on the top of the agenda of many French insurance market participants throughout 2017. It is worth noting that IDD aims to improve customer protection by changing insurance distribution standards, notably in strengthening pre-contractual information requirements (with clearer information provided to customers before taking out insurance products), expanding oversight and governance requirements by the implementation of product monitoring processes, introducing continuous professional training as well as preventing conflict of interest and promoting remuneration transparency.

2.3 Although there is a risk that the French ordinance implementing IDD may not meet the implementation deadline, it is our understanding that the French Treasury General Directorate (*Direction Générale du Trésor*) will use its best endeavours to submit a final draft to the advisory committee on the financial legislation and regulation (*Comité consultatif de la législation et de la réglementation financière*) by mid-November 2017. This constitutes the first step before the draft ordinance is submitted to the Ministers' council with a view to adopting the ordinance. The ordinance then needs to be ratified by the French parliament for the purpose of entering into force but on this timetable there is a reasonable chance that the implementation of IDD will be completed before the due date set out in the directive.

2.4 However, some French insurers have expressed particular concerns about how certain key provisions of IDD are proposed to be implemented into French law, notably as regards the appropriateness and suitability tests when providing advice on an insurance-based investment product ("**IBIP**") and the disclosure of inducements to customers. Indeed, as we understand that the first (non-public) draft ordinance circulated by the French Treasury General Directorate would have strengthened insurance distributors' obligations in this respect. More generally, the increased regulation brought in by IDD raises concerns from the French insurance market as regards the level of professional qualifications and ongoing training requirements and as to the delineation of responsibilities for mis-selling and other obligations between manufacturers of insurance products and distributors. Hence, particular attention should be paid to these areas where IDD ordinance is publicly released.

Insurtech

2.5 Concerning market dynamics, the development of Insurtech is also one of the major trends in force of this year. Digital innovations are creating new and unforeseen opportunities and challenges for insurers and regulators alike. For instance, blockchain is a rapidly emerging technology with the potential to streamline and transform many insurance interactions: a regulatory environment that is not sufficiently nimble and flexible to respond to these developments could significantly damage the growth prospects of the insurance industry. It is worth noting that more than a half of new French Insurtech start-ups have been set up during the last two years and some of them have already raised significant funds.

2.6 According to the *Autorité de contrôle prudentiel et de résolution* ("**ACPR**"), in its press release of 17 July 2017 announcing the strengthening of the ACPR Fintech Innovation Unit and the launch of two new communication actions for innovative financial players, financial investment and life insurance as well as non-life insurance remain dynamic sectors of the Fintech sector and account for 27% of innovative projects. This rapid emergence of new digital technologies and convergence with insurance disrupts the *status quo,* both for insurers and the regulatory authorities such as the ACPR supervising them.

2.7 The ACPR's latest publications show that they are well aware of the demands and growth opportunities which Insurtech can bring. The ACPR issued in November 2016 a recommendation on advertising financial products on social media. In this paper, ACPR recommends that firms, including insurance companies should adopt a number of best practices from 1st October 2017 including, without purporting to be exhaustive: to ensure that communications on social media (even if merely "shares") are fair and clear, that the advertising nature of the post should be explicitly indicated (if this is not clear from the message itself) and that content remains balanced, including with respect to the terms and conditions of a service or a product. Firms should implement internal control procedures over social media activities and should adopt monitoring measures to ensure compliance with internal procedures.

2.8 More generally, French insurers facing the current "maelstrom" of regulatory changes, notably those in connection with technology innovation, should consider adopting a new approach providing enterprise-wide coordination across core regulatory change activities to ensure consistency of approach to new regulations and to anticipate regulatory changes.

3. GERMANY

3.1 The German insurance industry is currently facing a number of challenges which call traditional business models into question and necessitate the development of new answers. Whilst the sector was still in the process of adapting to the era of Solvency II and delivered the first Solvency and Financial Condition Reports ("**SFCR**") and Regular Supervisory Reports, the German Government published a draft act for the implementation of IDD that would mean significant disruption for the German distribution system, prohibiting German brokers from accepting any remuneration from their retail customers. The industry associations were, however, successful in averting corporate realignment of the distribution market which was not required under IDD but rather increased consumer protection by increasing transparency of the remuneration structure. The German Act for the implementation of IDD has passed through parliament with sufficient time so that its provisions will come into force as required as of 23 February 2018.

3.2 Apart from these regulatory developments, insurers are confronted with new competitors that develop new products and distribution channels by making use of digitalisation. Insurtechs promise to serve the customers' interests better by offering individualised and flexible products at lower costs than the established insurance companies. Whilst insurers were sceptical in the beginning, they increasingly accept that a revision of their approach may be beneficial and now compete to cooperate with the newcomers.

Challenges for life insurers and potential solutions

3.3 The sector of the insurance industry which is currently undergoing the most challenging time in Germany is the life insurance sector. The coincidence of the introduction of Solvency II and a long-term low interest rate scenario has made the risks related to the traditional core product in the German market more transparent, the endowment policy with guaranteed interest, and has turned portfolios of such policies into a costly burden for insurers. Policyholders are increasingly dissatisfied as the surplus participation allocated to their policies decreases because the stock of high interest rate securities held by the insurers reduces as more and more of these securities mature and can only be replaced by investments with a lower rate of return. This process has been accelerated by a measure taken by the German legislator which obliges life insurers to build up additional reserves to ensure that the guarantees which were granted in the years of higher interest rates can be met. In order to build up such reserves (*Zinszusatzreserve*), insurers are forced to liquidate the hidden reserves related to their stock of high interest rate securities.

3.4 The solutions which life insurers are seeking include both changing the design of new products offered to the market as well as dealing with the existing portfolios. Insurers are launching a new generation of life insurance products which combine benefits based on the returns from capital markets investments as available under unit-linked policies but with reduced guarantees, such as a returning contribution guarantee in order to provide such protection for their customers investments. They are also looking for ways to decrease the costs of their existing portfolios.

3.5 German life insurers have been traditionally extremely hesitant to sell portfolios in external run-off transactions. Nevertheless, in the last decade, a number of so-called run-off platforms has been established which are supported by investors who expected that the introduction of the Solvency II regime might foster a demand from traditional insurers to get capital intensive portfolios off their books. About six portfolios have been transferred to these platforms, all of which stemmed from foreign insurers who have shut down their German business or from German insurers which have terminated their life insurance business entirely. These sellers were not concerned about the reputational consequences their step may have on the German life insurance market. Now for the first time, large German life insurers are openly considering putting their portfolios of traditional guaranteed life insurance policies into external run-off. This has immediately raised concerns of ongoing consumer associations and also other insurers that confidence of the customers might be severely impacted if insurers do not stand by their long-term contractual obligations but pass these to third parties.

3.6 Technically, an external run-off is executed by a portfolio transfer which basically is an asset transfer but is, in addition, subject to a regulatory framework, which most importantly includes the requirement of an approval of the transfer by the responsible regulator, in case of German insurance companies, the German Federal Financial Supervisory Authority ("**BaFin**"). The consent of each individual policyholder which would otherwise be required to transfer their policy, is replaced by the BaFin approval. In return, the task of BaFin is to protect the interests of the policyholders and to only grant the approval if their interests are preserved and evidence is provided that the obligations under the insurance contracts will continue to be met. The German Act on Insurance Supervision also contains safeguards that should ensure that the surplus participation of the policyholders is not affected by the transfer. However, as the return on such endowment policies in practice will only be determined over the remaining term of these policies, the impact of the transfer on such return is difficult to measure at the time of the transfer.

3.7 The other main aspects which BaFin needs to analyse before granting its approval are in particular the financial strength of the acquirer as well as the reliability and financial condition of the holders of significant participations in the acquirer. In light of the complexities related to the administration of the existing large portfolios of some of the established German life insurers, BaFin has stressed that it will also have an eye on the operational capacities of the acquirer.

3.8 Taking the obstacles into account that arise with a transfer of large portfolios, as well as the considerable risk that the trust of consumers in insurance companies that transfer parts of their portfolios to third parties will be severely damaged, external run-off may therefore be the tool of choice for large market players only under exceptional circumstances. However, as far as the smaller portfolios of these insurers that take a strategic decision to terminate a particular segment of business are concerned, run-off transactions have been and can be executed successfully and have proven to be a useful tool. In the light of Brexit, UK life insurers may also consider transferring their German portfolios while this is still possible under EU rules which allow for a transfer of such portfolios in accordance with the UK Financial Services and Markets Act ("**FSMA**").

4. HONG KONG

4.1 To modernize the insurance industry and bring Hong Kong in line with international practice, the government has brought a number of significant changes to the insurance regulatory regime in Hong Kong. The Insurance Companies (Amendment) Ordinance 2015 (Amendment Ordinance) was enacted on 10 July 2015 to amend the Insurance Companies Ordinance ("**ICO"**) to provide for the establishment of the independent Insurance Authority ("**IIA"**). The newly established IIA took over the statutory functions of the government department Office of the Commissioner of Insurance ("**OCI"**) on 26 June 2017 (D-day, as labeled by the government), marking the completion of the second stage of a three-stage regulatory reform. At the final stage, the IIA will take over the licensing and regulation of insurance intermediaries from the three intermediary self-regulatory organizations[5] in 2 years from D-day. The Amendment Ordinance will be renamed as the Insurance Ordinance ("**IO"**).

Key persons in control functions

4.2 One of the more significant developments under the IO is the introduction of the "key persons in control functions" concept consistent with the recent measures introduced by the securities and banking regulators in Hong Kong to heighten personal accountability for "management" of financial institutions. For an authorized insurer incorporated in Hong Kong, key persons are individuals holding positions that are likely to exercise a significant influence one or more of the insurer's control functions, including risk management, financial control, compliance, internal audit, actuarial and intermediary management. For authorized insurers incorporated outside Hong Kong, this is in respect of so much of its insurance business as is carried on within Hong Kong. The key person in a control function must be fit and proper and approved by the IIA. That approval can also be revoked. The fit and proper guideline (**GN4**) has been updated to reflect the new requirements such as the criteria for directors and key persons in control functions.

4.3 Being a key person comes with the prospect of personal liability; in the event that an offence is committed by an insurer, and it has proven that the offence was committed with the consent or connivance of an individual (being the controllers, directors, key persons in control functions or the members of the insurer), or attributable to any neglect or omission on the part of such individual, the individual also commits an offence.

4.4 One important point to note is that the offence works on a presumption basis, which means that the scope is very broad and captures individuals who are "concerned in the management" of the company. In other words, an individual can be presumed caught simply because he or she is part of the management of the company but this person may not be directly responsible for the actual offence committed by the company. In this respect, the IO goes further than its equivalent banking and securities ordinances.

5 These self-regulatory organizations ("**SROs**") are the Professional Insurance Brokers Association, The Hong Kong Confederation of Insurance Brokers and The Hong Kong Federation of Insurers.

Investigation and disciplinary powers

4.5 Compared to the OCI the IIA is much more powerful – the IIA has enhanced authorization and supervisory powers, as well as inspection, investigation and disciplinary powers over insurers, which largely modeled on the Securities and Futures Commission ("**SFC"**) regime. The IIA may impose a pecuniary penalty for misconduct of up to the greater of HK$10,000,000 or three times the amount profit gained or loss avoided by the insurers as a result of the misconduct. The IIA has published a new guideline (**GL18**) to set out the considerations that the IIA needs to take into account when they exercise power to impose pecuniary penalties on authorised insurers.

Insurance intermediary licensing regime

4.6 Another focus of the regulatory regime is the introduction of the new statutory insurance intermediary licensing regime. The IIA is currently in the process of preparing for the necessary tools, such as guidelines on conduct for regulating insurance intermediaries. The existing self-regulatory regime will continue until the IIA takes over the direct regulation of insurance intermediaries from the SROs in two years. When the new regime comes in, insurance intermediaries will be subject to more regulatory scrutiny by the IIA leading to a likelihood of an increase in compliance costs.

Tribunal

4.7 As part of the reform the Insurance Appeals Tribunal ("**IAT"**) was also set up to deal with appeals on the IIA's decisions to enhance the independence of the new regime. The IAT reviews specified decisions of the IIA including those on authorization, licensing and disciplinary actions.

Going forward

4.8 The IIA has introduced significant changes to the insurance regulatory landscape in Hong Kong, with a clear emphasis on the enhancement of responsibility and accountability for the conduct of insurance business in Hong Kong. Authorized insurers will need to implement changes in their policies and controls to align their governance, practices and processes with the new requirements.

4.9 Whilst it is uncertain how the IIA will exercise its new substantive powers in practice, the powers vested with the IIA are very similar to the existing powers of the SFC and the Mandatory Provident Fund Schemes Authority ("**MPFA"**). In this regard, we expect the IIA will likely reference the existing approaches of the SFC and MPFA in writing its guidelines and exercising its powers.

4.10 Apart from these regulatory changes, regulation of the Hong Kong insurance industry will continue to evolve as the IIA continues its work on the development of a risk-based capital regime and the introduction of a policy holders' protection scheme.

5. ITALY

5.1 The Italian insurance supervisory authority *Istituto per la Vigilanza sulle Assicurazioni* ("**IVASS"**) continues to make progress in the context of the implementation process of Solvency II and IDD. In the last twelve months, a good number of regulations and guidance has been published by IVASS. This legislation, which stems from the European legal framework and the recent changes made to Legislative Decree no. 209/2005 ("**Italian Insurance Act**"), is either intended to set out new second-level regulations or to be guidance addressed to players operating in the Italian insurance and reinsurance market. The main updates are summarised below.

Solvency II: the Italian implementation process continues

IVASS publishes regulation on intra-group transactions and risk concentration provisions

5.2 On 26 October 2016, IVASS published Regulation no. 30 dated 26 October 2016 laying down provisions concerning intra-group transactions and risk concentration, which implement the Italian Insurance Act as amended by Legislative Decree no. 74/2015. In particular, the Regulation gives full implementation to Articles 215-quarter, paragraph 2 and 216, paragraph 3 of the Italian Insurance Act and amends IVASS Regulation no. 25/2008. Moreover, the Regulation gives full implementation to two EIOPA Guidelines concerning the monitoring process on risk concentration (Guideline no. 68) and intra-group transactions (Guideline no. 69).

IVASS issues regulation on evaluation of assets and liabilities other than technical provisions

5.3 On 7 February 2017, IVASS published Regulation No. 34/2017, which is intended to set out a regime governing systems of governance and internal procedures for the evaluation by insurance undertakings of assets and liabilities other than technical provisions. In particular, the Regulation implements the EIOPA guidelines on the recognition and valuation of assets and liabilities other than technical provisions, pursuant to, amongst other things, Articles 30, 30-bis and 30-ter of the Italian Insurance Act. Regulation No. 34/2017 applies in particular to Italian insurance and reinsurance undertakings and to Italian branches of non-EEA insurance and reinsurance undertakings. These entities had to take the Regulation into account with respect to their financial statements given on 31 December 2016.

IVASS consults on draft regulation on insurance undertakings' and insurance groups' corporate governance systems

5.4 On 19 July 2017, IVASS published Consultation Document No. 2/2017, containing a draft regulation on insurance undertakings' and insurance groups' corporate governance systems intended to fully implement Solvency II, Delegated Regulation (EU) No. 35/2015 and the EIOPA guidelines on systems of governance.

5.5 The new regulation, when finalised and approved, will repeal and replace IVASS Regulation No. 20 of 26 March 2008 on internal control, risk management, compliance and outsourcing, IVASS Regulation No. 39 of 9 June 2011 on remuneration policies and IVASS Circular No. 574/2005.

5.6 Amongst other things, the new regulation has an impact on corporate governance, with particular regard to the role of corporate bodies, reinsurance together with other risk mitigation techniques, capital management, internal functions, remuneration policies, outsourcing and group governance.

IDD: Italian updates on the implementation process

IVASS consults on implementing preparatory guidelines on product oversight and governance ("POG")

5.7 On 11 January 2017, IVASS published a consultation paper on the application of preparatory guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors, which were issued by the EIOPA on 13 April 2016. The EIOPA guidelines are intended to support national competent authorities ("**NCAs**") and market participants with the preparation of the implementation of the requirements as laid down in IDD, which has a deadline for transposition by EU Member States of 23 February 2018. The preparatory guidelines require firms to:

(a) include appropriate steps to identify the group of consumers for whom a manufacturer is designing a product;

(b) align products with the relevant interests and objectives of the target market; and

(c) ensure the usage of appropriate distribution channels.

5.8 Manufacturers will also be required to properly test products before selling them to customers and take appropriate action to mitigate unforeseen risks that subsequently arise during the lifetime of the product. Insurers will also be required to strengthen control processes.

IVASS consults on insurance product information document

5.9 On 30 August 2017, further to the adoption by the EU Commission of Implementing Regulation (EU) No. 2017/1469 on the standardised presentation format for the insurance product information document ("**IPID**"), IVASS launched a consultation process intended to amend and integrate IVASS Regulation No. 35/2010 on transparency and advertisement. In particular, IVASS intends to simplify pre-contractual information by replacing the current informative note (*nota informativa*) with the insurance product information document as set out under the EU regulatory framework.

IVASS sets out recommendations on product oversight and governance arrangements

5.10 On 4 September 2017, IVASS published a letter to the market intended to provide some preliminary indications on the implementation of IDD and the steps to be taken by insurers and distributors in particular in the field of product oversight and governance arrangements.

5.11 The letter, after a brief introduction to the current status of the EU and Italian legal and regulatory framework, recommends that insurers and distributors promptly take any initial and necessary steps to adapt their internal models, procedures and policies in order to be ready to meet the new requirements set out under IDD as soon as this new piece of legislation comes into effect.

6. LUXEMBOURG

6.1 Luxembourg has an active insurance market and is widely recognised as a centre for the distribution of insurance products under EU rules on the freedom to provide services. The financial centre in Luxembourg currently hosts around one hundred insurance companies, mainly the subsidiaries of large international groups although this situation is expected to change following Brexit with further insurers choosing to headquarter in Luxembourg. Other notable developments in 2017 include several notices from the Luxembourg insurance sector supervisory authority, *Commissariat aux assurances* ("**CAA**") clarifying requirements in respect of acquisitions and increases of significant shareholdings, Solvency II reporting and IDD implementation.

Brexit

6.2 In its annual report for 2016/2017, the CAA reports that 2016 saw a positive development in terms of the activity and results of insurance and reinsurance undertakings in Luxembourg with balance sheets showing growth and an almost 46% increase in profits. Furthermore, the UK's decision to leave the EU was expected to have a significant impact on the Luxembourg insurance and reinsurance market as Luxembourg has seen a strong interest from large groups affected by Brexit wishing to relocate their EU activities.

6.3 According to the CAA 2016/2017 annual report, one group has already obtained a Luxembourg insurance sector authorisation, two others have submitted their application for authorisation and three others have announced their intention to do so. The CAA indicates that this could quickly result in doubling the non-life insurance activity in Luxembourg. Since the British referendum for leaving the EU, seven important industry players (AIG, Hiscox, Liberty, FM Global, CNA Hardy, RSA Insurance Group and Tokio Marine) have announced their intention to relocate to Luxembourg for their post-Brexit Europe operations.

Acquisitions and increases of significant shareholdings

6.4 The CAA has issued an information note on changes in the shareholding structure of insurance and reinsurance undertakings. In the information note, the CAA indicated that as of 1 October 2017 it will apply the new European supervisory authorities ("**ESAs**") Joint Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the financial sector (JC/GL/2016/01 of 20 December 2016) in respect of an assessment of qualifying holdings in insurance and reinsurance undertakings.

6.5 The main objective of the new Joint Guidelines is to provide the necessary legal certainty, clarity and predictability with regard to the assessment process contemplated in the sectoral directives and regulations. In particular, compared to the former 2008 joint guidelines of the predecessors[6] to the ESAs, the new Joint Guidelines in more detail:

(a) specify certain general concepts, such as those of 'parties acting in concert', 'indirect acquisitions of qualifying holdings', 'significant influence', 'decision to acquire', and the 'proportionality principle';

6 The Committee of European Banking Supervisors ("**CEBS**"), the Committee of European Securities Regulators ("**CESR**") and the Committee of European Insurance and Occupational Pensions Supervisors ("**CEIOPS**"),

(b) determine the assessment period and information to be provided to the target supervisor;

(c) clarify that where the notification is incomplete, the acknowledgment of receipt does not start the assessment period where the target supervisor either specifies the missing information in the acknowledgment of receipt, or refers therein to a separate letter to be sent in a reasonable timeframe thereafter; and

(d) clarify the assessment criteria for a proposed acquisition.

6.6 Finally, the new Joint Guidelines provide a recommended list of information to be required by the competent authorities for the assessment of an acquisition of a qualifying holding (which is an extended and modified list compared to the one annexed to the 2008 guidelines), as well as practical examples for the determination of acquisitions of indirect holdings.

Other Publications in relation to the Insurance Sector

6.7 The CAA issued several information notices and circulars over the last year focusing on reporting (in particular Solvency II reporting) matters (including the Information Note of 4 November 2016 and Circulars 16/10, 16/12, 17/1, 17/2, 17/3, 17/4 and 17/7) as well as Circular 16/9 on the deposit of securities and liquid assets used as assets representing technical reserves of direct insurance undertakings and Circular 17/6 on the exchange of collateral in relation to life insurance contracts where the investment risk is borne by the policyholder.

6.8 In relation to Luxembourg implementation of IDD, no implementing bill has been published so far. However, the CAA issued an Information Notice dated 20 July 2016 concerning the preparatory guidelines on the product oversight and governance arrangements of insurance undertakings and distributors published by EIOPA on 18 March 2016. The CAA informed EIOPA that it will fully apply the preparatory guidelines and invited insurers and insurance distributors to take all necessary measures to comply therewith by 23 February 2018, the date by which IDD has to be implemented.

7. SPAIN

As with many other European countries, Spain is preparing for the implementation of IDD. With the Catalonian political crisis, many insurance companies are moving their registered offices out of Catalonia. Both the implementation of IDD and the impact of the Catalonian political crisis on the insurance sector are discussed further below.

IDD

7.1 Following the requests of the insurance sector industry associations (such as Insurance Europe or the European Federation of Insurance Intermediaries ("**BIPAR**")) and the recent recommendation to the European Commission by the Committee on Economic and Monetary Affairs of the European Parliament ("**ECON**") on 17 October last to delay the application of IDD, it is not yet clear to what extent the application of IDD, which should be implemented by 23 February 2018 in all Member States (including Spain), will be delayed.

7.2 Despite the uncertainties surrounding a potential delay of the deadline, Spain is working to implement IDD by 23 February 2018. After a consultation procedure with the industry, the Spanish insurance regulator (the "**DGSFP**") sent a final draft bill implementing IDD (the "**Spanish IDD Draft**") to the Ministry of Economy before the summer. As soon as Spanish government endorses the Spanish IDD Draft (as amended, if applicable) the Parliamentary approval process will be initiated. It is difficult to determine the time schedule for parliamentary debate and approval with greater precision, since this calendar depends mainly on the date on which the Spanish IDD Draft is formally approved by the Government and some political decisions.

7.3 The Spanish IDD Draft generally follows the provisions of IDD in a quite literal way (especially those regarding information obligations and conduct rules) whilst maintaining some specificities of the Spanish market such as, for example, the traditional division between brokers and agents (including bancassurance operators, a subtype of agents).

7.4 The Spanish IDD Draft incorporates some other rules not related to the mere implementation of IDD, for example: (i) to impose the civil liability on insurers not only for actions of exclusive agents (as is the case in the current legislation) but also for actions of agents who act for several companies (so-called tied agents); (ii) the ability of banking networks to be split between several bancassurance operators (although probably of reduced application in practice taking into account the exclusivity provisions under bancassurance agreements); and (iii) the introduction of a regime of regulatory control of significant shareholdings in bancassurance operators (similar to the one currently applicable to insurance brokers).

7.5 The Spanish IDD Draft is not expected to "gold plate" IDD except in certain matters related to professional and registration requirements. Please note, for example, that a regulation implementing the Spanish IDD Draft is expected which will introduce training requirements in line with the ones currently in force and which are generally stricter than the ones included in IDD.

7.6 From a practical point of view, the key issue for the distribution industry will be how to adapt to new information obligations and conduct rules required by IDD. As opposed to other Member States, which had "gold plated" the current Insurance Mediation Directive in relation to conduct rules (as is the case with the UK), in Spain all these obligations will be new and will require a significant effort on the part of the industry to implement them.

7.7 Finally, it should be highlighted that the Spanish IDD Draft includes some transitional provisions which provide the industry with some additional time after the entry into force of the Spanish IDD Draft to adapt to its implementation, namely:

(a) Insurance distributors will have three additional months to comply with the new obligation and information rules;

(b) Insurers will have six additional months to comply with some of the new obligations regarding the registration of the person responsible for distribution, the internal register of employees who are involved in distribution activities and the new obligations regarding policies and internal procedures to guarantee the fulfilment of the fit and proper and training obligations; and

(c) Insurance intermediaries will have six additional months to adopt the requirement that customers' monies be transferred via strictly segregated customer accounts; and

(d) Insurance intermediary and distribution contracts relating to policies which entered into force before the Spanish IDD Draft is in force do not have to comply with it. However, in the case of renewal or amendment of policies entered into under such contracts, the Spanish IDD Draft will apply; in practice, this means that the distributors will have to comply with the relevant IDD obligations at the time of renewal or amendment of current insurance policies.

Insurance companies move their registered offices out of Catalonia

7.8 With the Catalonian political crisis many key players of the financial sector have rapidly changed their registered offices to other parts of Spain. Insurance companies are no exception: Axa Vida, SegurCaixa Adeslas, VidaCaixa, Catalana Occidente, Zurich or Allianz are all examples of companies that have also moved their registered offices out of Catalonia.

7.9 The change of registered office has been facilitated by the Spanish government, by means of the passing of a royal decree on October 6th 2017 to enable companies to change the location of their registered offices without having to seek the approval of a general shareholders' meeting (unless expressly required in their company by-laws) and, therefore, without having to wait for the minimum statutory notice to call a shareholders' meeting.

7.10 The first objective of this change of registered office is to guarantee that the nationality of these companies remains Spanish and, therefore, they are not at any time considered to be outside of the European Union and the internal market.

7.11 In relation to this issue it should be remembered that article 20 of the Solvency II Directive as implemented by article 30 of Spanish Law 20/2015, of July 14, on the management, supervision and solvency of insurers and reinsurers requires that the head offices or primary establishment of insurance or reinsurance undertakings must be situated in the same Member State as their registered offices. This means that in a theoretical scenario in which independence were recognized by Spain, the Spanish insurance regulator would require all of the insurance companies that have taken their registered office out of Catalonia to have their head offices or primary establishment in Spain. The Spanish Companies Act includes a similar requirement so one would expect that the companies who have moved their registered office out of Catalonia will start to comply with some of these requirements.

8. UAE

8.1 The rules for selling life insurance in the UAE (outside of the financial free zones such as the Dubai International Financial Centre ("**DIFC**")) are set to be fundamentally changed through a new regime currently in draft with the UAE Insurance Authority (the "**Insurance Authority**").

8.2 Over the past 12 months, the Insurance Authority has been in consultation with the market on its proposed rules. In April 2017 a revised set of draft rules was published and in May 2017, the final consultation period was closed. We now expect the final rules to be published shortly.

8.3 Based on the current draft, the rules will significantly impact all distribution channels, including bancassurance, with the following key categories of new requirements:

(a) **Commission restrictions** – strict limits on the commission which can be paid by the insurer to an intermediary will be introduced, calculated according to prescribed formulas will be introduced. This will reduce the overall commission levels available and also restrict the extent to which agents can receive commissions up front. Detailed definitions are proposed in the law to capture all forms of commission and there is even reference to an actuarial certification requirement to ensure commissions paid are in line with the regulations. Trail commissions may not be included in the total expense ratio ("**TER**") for mutual funds on investment products (or be otherwise included within charges passed on to investors).

(b) **Investor disclosures** – the new rules will seek to ensure that extensive disclosures are made to investors, especially in respect of savings/investment products. This includes detailed projections of returns and surrender values based on conservative estimates. Funds' disclosure must include historical performance of a selection of funds available to the investor (although it is currently unclear how risk and return metrics are expected to be described).

(c) **Cooling off period** – investors will benefit from at least a 30 day look back period to cancel and receive a return of cash paid. Projections must be given to investors without requiring full investor contact details and other personal information. All forms, including a number of new express disclosures on the nature of the investments, must be fully signed before the contract can be commenced and premium paid. Surrender values for investment products must be fair to the policyholder.

(d) **Bancassurance** – whilst the draft rules contemplate a two year "alignment period", bancassurance channels will be impacted for life products in the future and existing long term bancassurance agreements will need to be revisited; commission or premium mark ups at the point of sale by the bank will not be permitted. Bundling of credit life products with other financial services is also restricted and a separate arrangement for the insurance element must be documented. Banks must accept credit life protection from other providers when requested by the customer, even where they have an exclusive marketing arrangement with one particular provider.

(e) **Insurance intermediary registrations** – in addition to the existing licensing frameworks for brokers, a new licensing and qualification regime has been proposed for all intermediaries in respect of life insurance sales. This will seek to raise minimum standards. This is also proposed to be subject to a two year alignment period.

(f) **Product Regulatory Approvals** – all new programmes will need pre-approval from the Insurance Authority before being distributed. This will present an unclear hurdle from a timing and business certainty perspective, further increasing reluctance of firms to invest in arrangements to offer new investment products to the market.

8.4 Overall, the rules, once implemented, may contain some final changes but will certainly have a fundamental impact on the sale of life insurance in the UAE. By comparison to European initiatives, it may be a similar level of change to that affected by both the UK's Retail Distribution Review ("**RDR**")[7] and the EU Packaged Retail and Insurance-based Investment Products ("**PRIIPs**")[8] disclosure requirements being issued at the same time and only for insurers. Smaller intermediaries may be pushed out of business and larger intermediaries, including banks, may struggle to effectively sell investment contracts.

8.5 These rules will address significant market sentiment in the UAE that largely unregulated IFAs have been selling very complicated and expensive plans to vulnerable investors with limited options for redress.

8.6 With the UAE Securities and Commodities Authority also introducing new licensing requirements for foreign funds and the promotion of non-insurance investment products in recent months, investors may struggle to find easily accessible investment advice.

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7 RDR was launched by the Financial Services Authority, the predecessor body of the FCA, in 2006. The rules aimed to make the retail investment market work better for consumers. They raised the minimum level of adviser qualifications, improved the transparency of charges and services and removed commission payments to advisers and platforms from product providers.

8 Packaged retail investment and insurance products ("**PRIIPs**") are at the core of the retail investment market. They are investment products that are offered by banks or insurers to retail customers. In order to tackle consumer protection shortcomings for such products, the EU has adopted a regulation on PRIIPs, which obliges those who produce or sell investment products to provide investors with key information documents ("**KIDs**").

9. UK

9.1 There have been several significant developments in 2017 for the UK insurance sector, including the new UK regime for Insurance Linked Securities ("**ILS**"), regulatory progress towards recognising Insurtech innovation and moves towards national implementation of IDD – with all these developments being driven forward against a backdrop of continued uncertainty over the future of the UK's relationship with the EU following the 23 June 2016 Brexit vote.

Brexit

9.2 There is a substantial part of the UK press which paints Brexit as an epic constitutional, political and economic mess and there is a great deal of speculation as to whether the UK will be able to negotiate effective transactional measures and/or longer term effective solutions to provide financial services access to the EU Market. The current position is, undoubtedly, unhelpful to insurers based in the UK who wish to retain access to European markets, and to those currently entering the UK market from the EU who will need corresponding access to the UK market. Both groups are putting contingency plans into place and are starting to implement such plans now due to the uncertainty as to the nature of the final agreement to be reached between the UK and the EU and uncertainty surrounding a possible transitional period[9].

9.3 The lack of a clear, single solution for insurers to the myriad of problems that Brexit presents is also due to a lack of clarity on the issue to date by the UK regulators. The Prudential Regulation Authority ("**PRA**") has recently set out its Post-Brexit vision for insurance which shows some recognition of the potential problems, for example in respect of continuation of insurance contracts, although no solutions are yet provided.[10]

9.4 The UK regulator response to Brexit can be contrasted with the more proactive approach of EIOPA who, on 11 July 2017, published an Opinion on supervisory convergence in light of the UK withdrawing from the EU[11] (the "**July Opinion**") and so signalled the leading role that EIOPA will have in determining the approach to be adapted by EU regulators for UK (re)insurers looking to conduct business in the EU post-Brexit. Section 3 of the July Opinion made clear that it should not be possible for UK (re)insurers to establish a 'brass-plaque base' in an EU jurisdiction with a minimal number of employees that outsources all functions back to a UK-based (re)insurer. However, no specific requirements have yet been articulated. UK (re)insurers will therefore need to ascertain the regulatory approach of the jurisdiction in which they may decide to locate in the light of the principles set by EIOPA and may find that EU member state regulators who had earlier indicated a benign approach may have to impose more stringent requirements eventually.

9 For a discussion as to the impact of this in relation to Part VII insurance transfers of business, please refer to commentary by Ashley Prebble (Partner in the London Office) in the UK Financial Times Newspaper Insurers warned of risks to not completing Brexit plans, February 19 2017, article by Oliver Ralph, https://www.ft.com/content/afdfa8e0-f522-11e6-95ee-f14e55513608

10 Please refer to our briefing Post-Brexit vision for insurance: Sam Woods, Mansion House speech on geofinance, 20 October 2017 – https://www.cliffordchance.com/briefings/2017/10/post-brexit_visionforinsurancesamwoods.html

11 EIOPA-BoS-17/141 11.07.2017 – https://eiopa.europa.eu/Publications/Opinions/EIOPA-BOS-17-141%20Opinion_Supervisory_Convergence.pdf

9.5 As well as advising many of our clients both UK and EU based on their individual contingency planning, Clifford Chance London office has been advising the London Market Group ("**LMG**") Government Affairs Working Group and Brexit Taskforce. Our advice includes formulating the LMG views on transitional arrangements and a potential free trade agreement for the insurance industry post-Brexit. By having a presence on the Brexit Taskforce, Clifford Chance has been involved in leading responses to some of the major Brexit issues identified above and has helped generate a collective Brexit position amongst key players in the UK (re)insurance sector.

Insurance Linked Securities ("ILS")

9.6 Clifford Chance London office has also supported LMG legal advisers (the "**LMG's ILS Taskforce**") in consultations with the UK government and regulators to create a UK legal, regulatory and tax regime for ILS. The new regulations will include a new tax regime for ILS, a new corporate form, the Protected Call Company and a new approach to the approval and supervision of ILS issuers based in UK.

9.7 ILS is an alternative form of risk mitigation for (re)insurers. In contrast to conventional cover arranged with a reinsurance company, ILS offers (re)insurers a means of transferring risk to the capital markets. The ILS market is significant; with the UK government estimating that over $80bn of ILS has been issued as at 20 July 2017 with the figure set to grow to an estimated $87bn by 2019 and this is likely to be higher following the recent natural catastrophes in USA and the Caribbean. In light of London and the UK's pre-eminent position for catastrophe and speciality (re)insurance and the strength of the UK's capital markets and given the potential opportunities that ILS innovation could offer to the UK (re)insurance industry, in 2016 the UK government announced that it would explore options to attract ILS business to the UK.

9.8 The LMG's ILS Taskforce has been consulted by the UK government in the creation of this new ILS regime. Following their input, the government has made significant improvements to the proposed ILS legislation and simplifications to the proposed processes for regulatory approvals both of which will make the UK able to compete on a level playing field with more established ILS jurisdictions whilst ensuring that UK issued ILS arrangements will comply with the rules in Solvency II regarding special purpose vehicles and will therefore be attractive to EU cedants. For further information on the UK's ILS regime, please refer to our ILS briefings.[12]

12 A UK Framework for Insurance Linked Securities, 23 November 2016 – https://www.cliffordchance.com/briefings/2016/11/a_uk_framework_forinsurancelinkedsecurities.html; Update: UK insurance linked securities ('ILS') framework to be completed, 27 June 2017 – https://www.cliffordchance.com/briefings/2017/06/update_uk_insurancelinkedsecuritiesils.html; Update: Implementation of the UK's insurance linked securities framework moves closer, 16 October 2017 – https://www.cliffordchance.com/briefings/2017/10/update_implementationoftheuksinsuranc.html; PRA and FCA publish regulatory framework for insurance special purpose vehicles, 6 November 2017 – https://www.cliffordchance.com/briefings/2017/11/pra_and_fca_publishregulatoryframeworkfo.html

Insurtech

9.9 Insurtech, an offshoot of the financial technology (Fintech) sector, is a rapidly evolving movement aimed at simplifying and improving the efficiency of insurance by using blockchain technology and smart contracts.

9.10 Blockchain is a distributed ledger technology ("**DLT**") which allows the exchange of value or information in an entirely decentralised way, without intermediaries such as banks. This innovation draws on advances from a range of disciplines including cryptography (secure communication), game theory (strategic decision-making) and peer-to-peer networking (connections formed without central co-ordination). Each blockchain is underpinned by a 'smart contract' which holds the rules for processing any transactions made between participants. Smart contracts are comprised of automation or partial automation in code on a blockchain and contain the 'if that, then this' elements of the legal, business or contractual relationship between parties. Since the smart contract is on a blockchain, any update caused via an executed smart contract will be reflected in every node of the blockchain.

9.11 The FCA has taken the lead over the PRA in fostering proactive engagement in the Fintech and Insurtech space, principally through the launch of Project Innovate in October 2014. This project was designed to provide firms with the support necessary to navigate the regulatory system, while reducing barriers to innovation. As part of Project Innovate, the FCA launched a regulatory 'sandbox' where ideas could be created and tested, along with an advice unit, which opened in May 2016. The sandbox is a supervised space, open to both UK authorised and unauthorised firms and offers tools such as restricted authorisation, individual guidance, waivers and no enforcement action letters. Sandbox tests are expected to have a clear objective (e.g. reducing costs to consumers) and to be conducted small scale, so firms test their innovation for limited duration with a limited number of customers. The sandboxes are operated in a 'cohort' allowing for the testing of a limited number of proposals but many of which use blockchain and smart contract technology.

9.12 On 10 April 2017, with the aim of starting a dialogue with the industry, the FCA published DP17/3: Discussion Paper on distributed ledger technology.[13] In the discussion paper, the FCA confirms that as DLT is a new technology some of the products and business models it enables may require consideration of how specific regulatory requirements apply. Significantly, the FCA recognises that DLT has the potential to offer digitised assets that can be delivered directly to consumers, legal agreements that can be composed in software and enshrined in cryptographic layers, and secured data provenance for property or identity[14]. The FCA acknowledges that DLT's potential, combined with processing speed, might suggest that aspects of existing FCA rules may need to be reviewed in the light of this new technological context[15]. Additionally, the FCA appreciates that there will be certain legal questions which are matters for the courts to decide rather than being part of the FCA's remit – an example given – the conflict of laws issues regarding contracts executed on a DLT platform across multiple jurisdictions simultaneously.

13 https://www.fca.org.uk/publications/discussion-papers/dp17-3-discussion-paper-distributed-ledger-technology

14 Paragraph 1.16 of DP17/3

15 Ibid Paragraph 1.17

9.13 Following a speech entitled 'Enabling the Fintech transformation: Revolution, Restoration, or Reformation?' given on 17 June 2016 by Mark Carney, the Bank of England's "Fintech Accelerator" was launched. The Fintech Accelerator works in partnership with firms working with new technology to explore how Fintech innovations could be used in central banking – this is the only sector that has been considered by the Bank of England/PRA so far.

9.14 Clifford Chance is actively advising in the Insurtech sphere, including on the establishment of the Blockchain Insurance Industry Initiative ("**B3i**"). B3i intends to design and launch a reinsurance contract management platform utilising DLT and smart contracts to streamline the entry into and conduct of (re)insurance contracts. Our involvement in this innovative initiative underlines our ability to use our extensive UK and cross border multi disciplinary skills and expertise to support an important market development which will push the boundaries on insurance contract law and regulation.

IDD

9.15 Member States are required to transpose IDD into national law by 23 February 2018. Accordingly, the UK has moved towards adapting the existing IMD based legal and regulatory regime to ensure compliance with IDD. IDD will be transposed in the UK through the Financial Service and Markets Act 2000 ("**FSMA**") architecture in the same way as the transposition of IMD. This will involve a combination of amendments to legislation and to the FCA rules book. HM Treasury has issued a consultation paper, with the legislative changes expected to be made by the end of this year. Separately, the FCA has issued three consultation papers, as well as a policy statement with near-final rules. The FCA plans to publish all its final rules alongside the third policy statement, which is expected in January 2018.

9.16 IDD is a significant piece of legislation with implications for the EU insurance industry as a whole. However, as the UK already imposes higher standards than the IMD requires, the UK insurance industry is not expected to face as many changes as would otherwise be the case. Instead, many of the changes proposed by IDD will extend UK standards to other parts of the EU and where domestic provisions already exist, the FCA are likely to seek to minimise the disruption to UK firms.

9.17 Although the UK looks on schedule with its implementation of IDD, ECON has recommended that the application date for IDD be delayed until 1 October 2018[16]. If this recommendation is adopted by the European Commission, each EU member state would still be required to transpose IDD into its national legislation by 23 February 2018, but insurance intermediaries would not be required to comply with the new legislation until 1 October 2018. The ECON's recommendation has been made to enable the insurance industry across Europe has sufficient time to implement the technical and organisational changes which may be necessary to comply with the new legislation and regulatory requirements.

16 ECON has not published a press release on the recommendation. It appears from its webpage on the meeting, which was held on 16 October 2017 that ECON's request was included in recitals to recommendations on decisions not to objection to Commission Delegated Regulations made under the IDD.

10. US

10.1 Cybersecurity has been one of the key issues in 2017 for US financial service regulators in the insurance, banking and securities sectors. The three regulators: NYSDFS, NAIC and the SEC, are promulgating regulations and enforcement measures needed to prevent hacking, data breaches and exposure of confidential consumer and non-public information.

Nationwide Cybersecurity Regulation Is Coming

10.2 On October 24, 2017, the National Association of Insurance Commissioners ("**NAIC**") adopted the Insurance Data Security Model Law ("**Model Law**") following the "first ever" Cybersecurity Regulation (23 NYCRR Part 500) covering banks and insurance companies, issued by the New York State Department of Financial Services ("**NYSDFS**") in February 2017. Both the NAIC Model Law and the NYSDFS Cybersecurity Regulation require a written and implemented cyber security program and breach notification, which would set a nationwide standard for the insurance industry. Despite slight differences, the NAIC drafters emphasized that any Licensee in compliance with the NYSDFS "Cybersecurity Requirements for Financial Services Companies" will also be in compliance with the model law. NYSDFS, after the Equifax breach, has proposed expanding the cyber security regulations to cover credit reporting agencies.

10.3 The NAIC Working Committee expressed a preference for a uniform nationwide standard: "This new model, the Insurance Data Security Model Law, establishes standards for data security and investigation and notification of a breach of data security that apply to insurance companies, producers and other persons licensed or required to be licensed under state law. This model, specific to the insurance industry, is intended to supersede state and federal laws of general applicability that address data security and data breach notification. Regulated entities need clarity on what they are expected to do to protect sensitive data and what is expected if there is a data breach. This can be accomplished by establishing a national standard and uniform application across the nation." Following adoption by the NAIC, state legislatures need to pass legislation to implement the model law.

Key Requirements under the NAIC Model Law

10.4 A "Cybersecurity Event" is defined as "an event resulting in unauthorized access to, disruption or misuse of, an *Information System* or information stored on such *Information System*."

10.5 Each Licensee is required to develop, implement, and maintain a comprehensive written *Information Security Program* based on the Licensee's *Risk Assessment* which contains administrative, technical, and physical safeguards for the protection of *Nonpublic Information* and the Licensee's *Information System*. Governance oversight must be provided by the Licensee's Board of Directors or an appropriate board committee. The *Risk Assessment* should be commensurate with the size and complexity of the Licensee, the nature and scope of the Licensee's activities, including the Licensee's use of third parties to maintain, process, store or otherwise have access to *Nonpublic Information* through such third party's provision of services to the Licensee ("*Third-Party Service Providers*"), and the sensitivity of the *Nonpublic Information* used by the Licensee or in the Licensee's possession, custody or control.

10.6 The exercise of due diligence by the Licensee is required when selecting *Third-Party Service Providers*. In addition, Licensees must require *Third-Party Service Providers* to implement appropriate administrative, technical, and physical measures to protect and secure the *Information Systems* and *Nonpublic Information* that are accessible to, or held by, the *Third-Party Service Provider*.

10.7 A written incident response plan designed to promptly respond to, and recover from, any Cybersecurity Event that compromises the confidentiality, integrity or availability of *Nonpublic Information* in the Licensee's possession, the Licensee's *Information Systems*, or the continuing functionality of any aspect of the Licensee's business or operations must be in place.

10.8 An annual written statement, certifying that the insurer is in compliance with the *Information Security Program* requirements must be submitted by each insurer to the chief insurance regulatory official of the state. All records, schedules and data supporting the certification must be maintained for a period of five years for examination by the appropriate insurance regulatory body.

10.9 If a Cybersecurity Event has or may have occurred, an investigation must be conducted by the Licensee and the Commissioner must be notified as promptly as possible, but no later than 72 hours from a determination that a Cybersecurity Event has occurred. Notice is also required for Cybersecurity Events affecting systems maintained by *Third-Party Service Providers* and reinsurers.

10.10 Additionally, the Model Law includes confidentiality protections for certain information provided to an insurance regulator or as a result of an investigation or examination pursuant to the Model Law from disclosure requests under state freedom of information, "open records", "sunshine" and other similar laws.

10.11 On the federal level, the SEC has announced the creation of a Cyber Unit which joins existing units within the Enforcement Division. The Cyber Unit is part of an evolution of the SEC's efforts to ensure market intermediaries and public companies work diligently to safeguard confidential customer information and protect the integrity of the securities markets. Experts believe the initial cases may arise from technical violations, such as: (1) failure to have robust cybersecurity policies and procedures, failure to follow existing cybersecurity policies and procedures, and failure to establish appropriate controls; (2) failure to perform sufficient periodic assessments of cyber procedures and measures, and failure to respond to deficiencies learned through assessments of a prior breach; and (3) failure to protect networks containing *non-public* customer information with appropriate technology (e.g., firewalls, encryption, anti-virus software) and reasonable procedures (e.g., access controls).

How can we help?

Clifford Chance are a trusted advisor to the world's leading insurers and reinsurers on complex transactions, disputes, financing, regulatory and commercial matters. Our international team of over 200 fee-earners offers first class domestic and cross-border advice across the world's main financial centres and the emerging markets.

We support our clients across the full range of their legal needs including: M&A and joint ventures, establishing new operations, restructuring and run-off, financial services regulation and enforcement, development of complex insurance products, raising capital, reinsurance and alternative risk transfer, distribution, major insurance/reinsurance disputes, outsourcing and other commercial contracts.

We are a recognised leader in the global insurance sector. In the Chambers UK 2018 rankings we have maintained our Tier 1 ranking in Insurance: Non-contentious and we were also awarded 'Legal Firm of the Year' 2017 by Reactions, a magazine for the global insurance and reinsurance market.

If you require further information on any particular topic referred to in this publication generally, please do not hesitate to get in touch – our contact details can be found at the end of this publication.

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