# Module I Unit 16B

## BUSINESS CONDUCT, ETHICS AND ESG

**Purpose**

At the end of this unit the participant should be able to demonstrate an understanding as to the key values and behaviours which constitute business ethics and the associated regulatory requirements for insurers to follow so as to conduct business in accordance with those values. , As well the participant will have an awareness of the GIIA initiative to raise the profile of Environmental, Social and Governance (ESG) factors in the insurance industry.

**Assumed knowledge**

None

| **Summary of learning outcomes** |
| --- |
| 1. Explain the importance of business ethics. |
| 2. Explain the 10 Principles for the Conduct of Finance Business. |
| 3. Explain the reasons why Commercial General Insurers are required to comply with more prescriptive rules. |

# Module I Unit 16B

## BUSINESS CONDUCT, ETHICS AND ESG

### 16.0 BUSINESS ETHICS AND CONDUCT

Business ethics are the values, culture and principles that are adopted to set the standards and behaviours that will be applied in a company's decision making, its dealing with stakeholders and its day to day operations.

Honesty, fairness, integrity and respect are examples of the ethical values to which a company may want to commit.

The role of the Board is vital in building and maintaining an ethical culture, and in the development of a governance framework and policies that set standards of conduct for the Board, for individuals within the company and for the conduct of the organisation as a whole.

An ethical culture applies to any and all aspects of business conduct, including:

- Fair treatment of customers
- Regulatory compliance
- Open communication
- Conflicts of interest
- Bribery & corruption
- Gifts and hospitality
- Procurement
- Discrimination and diversity

Detailed policies and procedures for the above elements of business conduct should be put in place by the insurer to enable its day to day operations to be carried out in compliance with the company's business ethics.

Training of staff is important as well as whistleblowing processes for staff to comfortably be able to raise concerns and report breaches of the procedures without fear of reprisal.

The staff are the first line of defence in ensuring compliance with the company's policies and the second line of defence – the Compliance Officer (or MLRO if appropriate) - will be the first port of call for staff to report concerns or breaches.

Module I Unit 15 Compliance sets out how the insurer's compliance function and framework should be designed to ensure that the company develops an appropriate compliance culture, policies and procedures and provides training, monitoring and board reporting.

### 16.1 REGULATION OF BUSINESS CONDUCT

The GFSC has issued various rules, codes and guidance relating to the business conduct of insurers.

The Insurance Business Rules and Guidance, 2021 include, as Schedule 2, 'The Principles of Conduct of Finance Business'.

Licensed insurers are required to ensure that these 10 principles are incorporated into their business culture and practices, and into their documented policies and procedures:

**1. Integrity** - A licensee should observe high standards of integrity and fair dealing in the conduct of its business.

**2. Skill, Care, and Diligence** - A licensee should act with due skill, care, and diligence towards its customers and counterparties.

**3. Conflicts of Interest** - A licensee should either avoid any conflict of interest arising or, where a conflict arises, should ensure fair treatment to all its customers by disclosure, internal rules of confidentiality, declining to act, or otherwise. A licensee should not unfairly place its interests above those of its customers and, where a properly informed customer would reasonably expect that the firm would place their interests above its own, the firm should live up to that expectation.

**4. Information about Customers** - A licensee should seek from customers it advises, or for whom it exercises discretion, any information about their circumstances and investment objectives which might reasonably be expected to be relevant in enabling it to fulfil its responsibilities to them.

**5. Information for Customers** - A licensee should take reasonable steps to give a customer it advises, in a comprehensible and timely way, any information needed to enable them to make a balanced and informed decision. A licensee should similarly be ready to provide a customer with a full and fair account of the fulfilment of its responsibilities to them.

**6. Customer Assets** - Where a licensee has control of, or is otherwise responsible for, assets belonging to a customer which it is required to safeguard, it should arrange proper protection for them, by way of segregation and identification of those assets or otherwise, in accordance with the responsibility it has accepted.

**7. Market Practice** - A licensee should observe high standards of market conduct and should also comply with any code of standard as in force and issued or approved by the Commission.

**8. Financial Resources** - A licensee should ensure that it maintains adequate financial resources to meet its finance business commitments and to withstand the risks to which its business is subject.

**9. Internal Organisation** - A licensee should organise and control its internal affairs in a responsible manner, keeping proper records, and where the firm employs staff or is responsible for the conduct of finance business by others, should have adequate arrangements to ensure that they are suitable, adequately trained and properly supervised and that there are well-defined compliance procedures.

**10. Relations with Guernsey Financial Services Commission** - A licensee should deal with the Commission in an open and co-operative manner and keep the regulator promptly informed of anything concerning the firm which might reasonably be expected to be disclosed to it

**Retail Insurance Business**

The protection of retail insurance customers is seen by the GFSC as carrying a higher degree of risk than for corporate insurance buyers, as retail customers are deemed to be less knowledgeable or ‘sophisticated’ than corporates in assessing the suitability and competitiveness of insurance products that they wish to buy. The GFSC has therefore issued more prescriptive rules and guidance as to how they expect the principles of business conduct to be put into practice by insurers when dealing with retail customers.

Part 7 - Conduct of Business of The Insurance Business Rules and Guidance, 2021 applies to all Category 1 (Commercial Life) and Category 3 (Commercial General) licensed insurers with respect to business with retail customers. Commercial insurers must have policies and procedures in place to incorporate these rules and guidance into their business practices.

- Applying due skill, care and diligence when dealing with customers
- Fair treatment of customers
- Identification and avoidance or management of conflicts of interest
- Ensuring the fair treatment of customers in their dealings with intermediaries, by using only properly licensed intermediaries with the necessary knowledge, skill and resources who comply with the applicable laws and regulation.
- Development and distribution of insurance products which takes into account the interests of different types of consumers, with thorough assessment of the main characteristics of a new product to ensure that it meets the needs of the target market, and is only promoted to the target market to avoid misselling.

- Promotion of products and services in a manner that is clear, fair and not misleading.
- Provision of timely, clear and adequate pre-contractual and contractual information to customers so that they can make an informed decision about buying and understand their rights and obligations after sale.
- Advice provided to customers by the insurers or the intermediary takes into account the customer's disclosed circumstances, to avoid misselling.
- Appropriate servicing of policies throughout the life of the contract until all obligations have been satisfied, including disclosure of all relevant information about the policy and changes in the insurer's details or the policy terms and conditions.
- Timely, fair and transparent claims handling
- Timely, fair and transparent complaints handling

**Board Conduct**

The required standard of conduct of the individual board members of licensed insurers is set out in Principle 4 of Appendix 3 of the GFSC's Finance Sector Code of Corporate Governance. This is explored in detail in Unit 16A Module 1 – Governance.

### 16.2 ENVIRONMENTAL, SOCIAL AND GOVERNANCE – ESG

Organisations are facing growing demands from stakeholders for clear and transparent disclosure of their environmental, social and governance (ESG) strategy and how they are managing their commitment to ESG factors such as sustainable supply chains, renewable energy, limiting greenhouse gases, diversity and inclusion, good health & wellbeing and fair trade.

Insurers recognise that proper understanding and integration of ESG factors is increasingly critical to the long-term viability of their businesses. ESG-related criteria have moved from a 'peripheral' concern to a 'core' issue across all sectors, and this includes insurance.

**GIIA ESG Framework**

The Guernsey International Insurance Association ("GIIA") has developed the world's first Environmental, Social and Governance ("ESG") Framework for insurers.

The central feature of the Framework is the United Nation's ("UN"s) 17 Sustainable Development Goals ("SDG"s). Adopted by all UN Member States in 2015, the SDGs provide a shared blueprint for peace and prosperity for people and planet and represent the most widely accepted benchmark for ESG.

In developing the Framework GIIA is seeking both to recognise and validate the work Guernsey insurers are already doing but also to provide a "handrail" to enable all Guernsey insurers to start a conversation about their impact on people and planet and consider adopting their own ESG Policies.

The Framework is compiled of four pillars:

**Pillar 1 - Governance Principle: ESG is embedded within decision making and the governance structures of the insurer**

The governance and decision-making processes of the insurer must consider how the Insurer contributes to achieving the SDGs. The insurer or its appointed insurance manager must be a member of a representative body that is a signatory to UN's Principles of Sustainable Insurance or is a member itself.

**Pillar 2 - Risks Underwritten Principle: Risks underwritten by the Insurer must contribute to achieving the SDGs either directly or by supporting policyholders to indirectly achieve the goals.**

The insurance policies sold by the insurer either directly or indirectly support the achievement of the SDGs. The six SDGs most commonly supported through the issue of insurance policies by Guernsey Insurers are meeting basic needs, wellbeing, decent work, resource security, healthy ecosystems and climate stability.

**Pillar 3 – Investments Held Principle: Investments held contribute to achieving the SDGs.**

Investments of the insurer must be held or managed by a financial institution with a good or better ESG rating.

**Pillar 4 - Reporting Principle: transparency is at the heart of the framework.**

The insurer must disclose publicly, at least annually, how it has met the requirements of the Framework.

Insurers are able to develop and adopt an ESG policy which will allow the company to self-certify adherence to the GIIA Framework.

Insurers can also then apply for external accreditation from ESI Monitor, GIIA's third party ESG partner, and the insurer can use the Kitemark once their policies have been validated.

The desire of the board to develop and certify ESG policies is likely to reflect the attitude towards, and reporting requirements in respect of, ESG within the insurer's larger group, The boards of insurers are therefore likely to develop ESG policies in coordination with those responsible for ESG policies at shareholder level.

**Green Discount for Life Insurers**

Regulators have recognised that they have a responsibility for financial stability, which includes the need to help mitigate the adverse financial impacts of climate change.

In December 2020 the GFSC amended the Insurance Business (Solvency) Rules 2015 with the introduction of a 'Green Discount' to incentivise increased investment in 'Green Assets' by life insurers and thereby help promote positive environmental outcomes.

A Category 1 or 2 life insurer can take a Green Discount of up to 15% in the calculation of the PCR for Green Assets.

Green Assets relate to investment in activities which meet the criteria set out in The Common Principles for Climate Mitigation Finance Tracking, including renewable and efficient generation and use of energy, agriculture forestry and land use, greenhouse gas reduction, waste and wastewater and transport.

The change in the Solvency Rules enables insurers to purchase Green Assets in the knowledge that long-term Green Assets are considered suitable to meet long-term liabilities whilst maintaining policyholder protection.

**Self-test questions**

Answering these questions will remind the participant as to what has been learnt. Once completed, please check your answers against the relevant text.

1. How should the board of a licenced insurer behave when dealing with the GFSC?
2. Name three procedures that a Commercial General Insurer is required to establish and follow?
3. Is a Guernsey (re)insurer required to adopt an ESG framework?
4. What is the Green discount?

| Summary of learning outcomes |
| --- |
| 1. Explain the importance of business ethics. |
| 2. Explain the 10 Principles for the Conduct of Finance Business. |
| 3. Explain the reasons why Commercial General Insurers are required to comply with more prescriptive rules. |