Module K Unit 20

LONG TERM BUSINESS

Purpose

At the end of this unit the participant should understand the nature of Long term business conducted in Guernsey and how management of this business differs from General insurance and Employee Benefits.

Assumed knowledge

An understanding of Customer Due Diligence and AML/CFT requirements as described in Unit 15

Summary of learning outcomes
1. Describe the types of risk and insurance policies that make up long term business.
2. Explain why the regulation of long-term business is more onerous than General insurance.
3. Explain the importance of conducting, maintaining and refreshing customer due diligence records by applying great care and attention.
4. Demonstrate an understanding of The Insurance Business Rules & Guidance 2021, Part 7.
5. Explain the role and powers of the Channel Islands Financial Ombudsman (CIFO).
6. Describe the key requirements contained within the Guidance Notes for Life & Pension business

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20.0 INTRODUCTION

Guernsey has an International Life Assurance sector which conducts various types of Life and Investment business exclusively with (non-domestic) overseas customers. The size and nature of this business warrants separate consideration from the General Insurance and Employee Benefits businesses written by captive insurance companies.

20.1 THE INSURANCE BUSINESS (BAILIWICK OF GUERNSEY) LAW, 2002

20.1.1. Long term business and general business.

For the purposes of the Law, insurance business, including domestic business, is divided into either long term business or general business.

a. Long term business is defined as insurance business of any of the descriptions set out in Schedule 1, which can be located at page 211/270 of the law. See page 233 at https://www.guernseylegalresources.gg/CHttpHandler.ashx?id=71522&p=0%20
b. General business means insurance business other than long term business.
c. the effecting or carrying out of a contract whose principal object is set out in Schedule 1 irrespective of any subsidiary provisions which are not within it, shall be taken to constitute long term business.
d. Notwithstanding the provisions of subsections (a), (b) and (c) a licensed insurer may elect to regard a contract of insurance on human life expressed to be for a term of not more than 18 months as general business; and if so elected, it shall not for the purposes of this Law be taken to constitute long term business.

To summarise, long term business is generally life related, including contracts of insurance on human life, longevity based annuities, contracts to provide sums on marriage or birth, contracts linked to indices of property values, permanent health insurance, capital redemption contracts, pension fund management and credit life assurance. This is a synopsis rather than exhaustive list. Generally, long term business will also include life indexed derivatives and reinsurance of those types of risk. Long term business carries greater risks in terms of prudential management and therefore usually carries enhanced customer protection, accounting, actuarial and capital requirements than general business.

Generally, the approach to regulating Life and General insurers is very similar; however, the following are specific to Life business only:

a. Special requirements in respect of insurers with long term business

   Appointment of actuary
   The Law requires the licensee to appoint an Actuary, who must be approved by the Commission prior to the appointment taking effect.

   Actuarial valuation
   The Annual Return Regulations require an actuarial valuation prepared by the company's actuary to be submitted with the annual return, although more frequent valuations may be requested if considered necessary.

   Separation of assets and liabilities attributable to long term business
   A licensed insurer which carries on long term business shall maintain such accounting and other records as are necessary for identifying:

I. the assets representing the fund maintained by the insurer and each part of that fund,

and

II. the liabilities attributable to that business and to each part of that business.

Restriction on transfer of assets of insurer with long term business

A licensed insurer is permitted to settle claims and expenses in relation to the business; however is only allowed to transfer assets representing the fund maintained by the insurer to the shareholder, out of any established surplus in the fund, after any deficits have been eliminated

Transfers of long term business

A scheme under which all or any of the long term business is to be transferred to a third party shall not be carried out without the sanction of the Royal Court.

b. Other requirements

20.2 POLICYHOLDER PROTECTION

Guernsey registered international life and pension's insurers must comply with the policyholder protection requirements. These requirements include the appointment of a Guernsey based trustee who may in turn appoint a custodian to hold the company's assets, if the Trustee is unwilling to hold the assets. Assets representing at least 90% of policyholder liabilities must be held in trust. Full details of the Guernsey policyholder protection requirements are contained in the standard condition imposed under section 12 of the Law on the licences of companies writing long term business.

20.3 ANTI-MONEY LAUNDERING & COUNTERING FINANCING OF TERRORISM REQUIREMENTS

The licensed entity must put in place an Anti-Money Laundering (AML) & Countering Financing of Terrorism (CFT) Manual to provide its employees and those undertaking the entity's business with the information needed to comply with both its own obligations in relation to the Commission's Handbook and the associated AML/CFT legislation. It should cover the key aspects that need to be documented in accordance with the Bailiwick of Guernsey's AML/CFT framework.

As a result, the licensee is required to carry out customer due diligence requirements (CDD) in respect of each policyholder as part of its take-on process. It should be noted that entities when assessing the client risk at take-on should also take in to consideration tax evasion, bribery and corruption and fraud.

Please refer to Unit 15 Compliance, where AML/CFT is discussed in greater detail

20.4 THE INSURANCE BUSINESS RULES & GUIDANCE 2021, PART 7

The rules require that policyholders/clients are dealt with in a fair and transparent manner and treated fairly. The following details the requirements of the rules at a high level, however, please revert to the Rules to establish a greater understanding of its detailed requirements. However, as a result a licensed insurer must:

- act with due skill, care and diligence and have policies and procedures in place to ensure that employees and agents meet high standards of ethics and integrity when dealing with customers;
- establish and implement policies and procedures on the fair treatment of customers and adopt the fair treatment of customers as an integral part of their business culture, with policies and procedures supporting this objective being properly embedded in the organisation;
- seek to avoid or properly manage any potential conflicts of interest;
- have arrangements in place when dealing with intermediaries to ensure the fair treatment of customers and have procedures in place to verify that the intermediaries have the appropriate qualification, knowledge and ability to distribute the licensee's products; incorporating a terms of business agreement completed and signed by the intermediary;
- ensure that the interests of different types of consumers are considered when developing and distributing insurance products;
- promote products and services in a manner that is clear, fair and not misleading;
- provide timely, clear and adequate pre-contractual and contractual information to customers and take reasonable steps to ensure that a customer is given appropriate information about a product in order that the customer can make an informed decision about the arrangements proposed;
- ensure that any product documentation includes key features information as required by the COBs rules;
- must take into account the customer's disclosed circumstances, irrespective of whether the advice is being given by the licensee or an intermediary;
- service policies appropriately through to the point at which all obligations under the policy have been satisfied and to ensure the provision of relevant information to customers throughout the life of the policy;
- ensure that any Information provided on an ongoing basis, including changes in policy terms and conditions or amendments to the legislation applicable to the policy;
- ensure timely, fair and transparent claims handling and claims dispute resolution policies and procedures are in place.
- ensure that if the licensed insurer outsources, any of the claims handling processes, it remains ultimately responsible for the provision of fair and transparent claims handling and claims dispute resolution and compliance with the Rules;
- handle complaints in a timely and fair manner and ensure compliance with, a written procedure for the effective consideration and fair and proper handling of any complaints relating to the licensed insurer's insurance business, howsoever received
- adhere to the requirement to maintain a complaints register and file reports with the GFSC in accordance with the requirements of the COBs rules

20.5 CHANNEL ISLANDS FINANCIAL OMBUDSMAN (CIFO)

CIFO is the joint operation of two statutory ombudsman roles, established in law by the Financial Services Ombudsman (Jersey) Law 2014 and the Financial Services Ombudsman (Bailiwick of Guernsey) Law 2014.

The primary role of CIFO is to resolve complaints arising from financial services provided in/or from the Channel Islands of Jersey, Guernsey, Alderney and Sark.

CIFO handles enquiries from complainants and financial services providers, to help them resolve issues between themselves, and to intervene in cases based on misunderstandings. It will try to resolve the case by mediation; helping the parties to reach a fair settlement. If mediation is unsuccessful, CIFO will investigate the case and issue a decision. If the complainant accepts the decision, it becomes legally binding on both parties. The ombudsman can award compensation, payable by the financial services provider, up to a maximum limit of £150,000.

20.6 GUIDANCE NOTES FOR LIFE & PENSION BUSINESS

The legal requirements are set out in the Insurance Business (Bailiwick of Guernsey) Law, 2002, as amended ("the Law"), and the associated regulations, rules and codes.

20.6.1 Business Plan

All registered life companies are required to submit a business plan annually, covering the previous year and at least the next 3 years, to include the following information:

- a summary of the products being offered and the markets in which these products are being offered;
- forecast business volumes for each type of product;
- levels of retention of life cover;
- details of reinsurers;
- unaudited financial projections, including the breakdown of expenses; and
- details of the operation of the policyholder protection arrangements.

The Commission should be informed prior to any material deviation from the business plan.

20.6.2 Annual Insurance Return

The Annual Insurance Return is due within four months of the financial year end of the insurer.
Details of the requirements for annual returns are contained in The Insurance Business Rules and Guidance 2021 Part 3 (Annual Return) a copy of which can be found in the 'Legislation and Guidance' section of the Commission's website. In certain circumstances, more frequent returns may be requested. These returns would normally take the form of a set of management accounts to enable an evaluation to be made as to the volumes of premium income, level of reserves, assets and levels of expenses. It may also be necessary to produce a letter of comfort from a parent and/or provide additional information from the auditor or actuary.

20.6.3 Actuarial Declarations

The Annual Return Regulations require an annual declaration signed by the Actuary regarding the products being sold and policyholders' expectations to be submitted with the annual return. An additional declaration is to be supplied in advance of the launch of any new product. Copies of these declarations are contained in the 'Documents and Forms' section of the Commission's website.

The investment funds to which life assurance products are normally linked (whether internal or external) will continue to be reviewed once a year. However, to avoid any potential issues, it is advisable for a life assurance company to submit details of any unusual proposed linkages (e.g. external indices, derivatives or property) before these are entered into.

20.6.4 Duties of the External Auditors

The duties of the external auditors include reporting on the adequacy of the systems of internal control operating within the company, which for a life and pensions insurer should cover:

- the process for ensuring that the degree of mismatching of assets and liabilities is minimised;
- the process for monitoring the breakdown of expenses;
- the process for establishing policy reserves and transferring assets to and from the control
- the continuing suitability of the method adopted for unit pricing and the administrative
- a copy of the auditors' management letter, including details of any weaknesses, must

20.6.5 Agents

The actuarial declarations mentioned above should extend to all literature issued by agents, whether tied or independent. In relation to investments selected by agents, the actuary and the General Representative should satisfy themselves that no unreasonable claims, particularly in relation to investment potential, are made. The company should monitor all literature issued by agents and ensure that all agents are aware of this requirement.

20.6.6 Public Disclosure

All insurance companies licensed in Guernsey are subject to The Insurance Business Rules and Guidance 2021 – Part 4 (Public Disclosure). Applicants should agree the details of the required public disclosure of financial information with the Commission.

20.6.7 Outsourcing

It is not uncommon for life assurance entities to delegate a significant part of the day-to-day administration to the parent and/or one of its subsidiaries as it usually has the required expertise, knowledge and skills along with the appropriate systems and controls in place to administer the business and therefore is better positioned to deliver this function.

The Finance Sector Code of Corporate Governance requires that an insurer retains at least the same degree of oversight and accountability for any outsourced material activity or function as applies to non-outsourced activities or functions.

The outsourcing relationships should be governed by written contracts that clearly describe all material aspects of the outsourcing arrangement, including the rights, responsibilities and material expectations of all parties. Therefore the Board and/or Senior Management should consider:
- how the insurer's risk profile and business continuity will be affected as a result of the outsourcing;
- the service provider's governance, risk management and internal controls and its ability to comply with applicable laws and regulations;
- the service providers' service capability and financial viability; and
- succession issues to ensure a smooth transition when ending or varying an outsourcing arrangement.

These arrangements should be subject to periodic review and the board and/or senior management reported to on a regular basis as to the outcome of review process, as the board remains responsible and accountable in respect of functions or activities that are outsourced.

20.6.8 Own Risk & Solvency Assessment ("ORSA") and Own Solvency Capital Assessment ("OSCA") for Guernsey insurance Companies

Under the Insurance Business (Solvency) Rules & Guidance, 2021 insurance and reinsurance companies licensed in Guernsey are required to assess and monitor their regulatory solvency requirements under a risk-based framework.

The Rules require licensed insurers to hold sufficient capital resources to meet both the Minimum Capital Requirement and the Prescribed Capital Requirement, the latter being calculated using principles similar to the Solvency II standard formula for determining the Solvency Capital Requirement.

The directors of Guernsey insurance companies are also required to determine, with justification, their own view of the appropriate level of capital resources for solvency purposes. For this purpose, each company must undertake a periodic review of the risks to which it is exposed by carrying out an ORSA.

This approach is similar to requirements for insurers located within the European Union who must comply with requirements to meet both a Minimum Capital Requirement and a Solvency Capital Requirement, and also prepare an ORSA in line with Solvency II requirements.

Guernsey insurance undertakings are required to conduct an ORSA at least annually and whenever a change to the company's business plan will have a material impact on the company's solvency position. The ORSA report must also be submitted to the Guernsey Financial Services Commission.

The ORSA must include the directors' assessment of the company's current and projected solvency positions. It must also include a quantitative and qualitative assessment of the company's risk exposure along with stress and reverse stress tests of its solvency position.

For certain classes of insurer, including PCCs and commercial reinsurers, the Rules permit a company to limit its ORSA to an assessment of its current solvency position, known as an OSCA.

As for a full ORSA, an OSCA must be prepared at least annually and an OSCA report submitted to the Commission. The OSCA must address the risks considered within the regulatory solvency calculation, as well as other risks which may be material to the insurer, including liquidity and operational risk.

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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. Name three types of Long term coverages and an Employee Benefits cover that is not regarded as Long term business for regulatory purposes? 2. Name three special requirements of an insurer writing Long term business? 3. What action must be taken with regard to Policyholder Protection? 4. Why is customer due diligence so important when conducting Long term business? 5. When does an award by the Financial Ombudsman become legally binding on the insurer? 6. What is an ORSA and what must it include?

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