# Ethics in Insurance: the challenges ahead in 2018

By Duncan Minty 30th November 2017

What does 2018 hold for the insurance sector? Certainly much talk about start-up firms and challenging the incumbents. And a challenging rating environment and some significant pieces of legislation as well.

So what should we look out for in terms of ethics?

I think 2018 will be an eventful time for the ethics in insurance, and in this post, I'm going to outline what I think will represent the big challenges. I'll start with those two significant pieces of legislation, the Senior Managers and Certification Regime (SMCR) and the General Data Protection Regulations (GDPR)

## Remember the Forest

?The SMCR and the GDPR are going to focus a lot of attention on the building and strengthening of compliance and accountability frameworks within UK insurance firms. Yet the great attention to detail these two regulations will bring about will in itself present dangers, of focusing too much on the trees and not enough on the forest.

There's a danger that all that attention to regulatory detail will cause some big accountability issues to be lost sight of. I raised some of these in a post last September (more here), in which I identified seven components of a 'great accountability challenge', driven in large part by the automation of insurance decision making. The key question therefore is whether insurers will connect the detail of their SMCR and GDPR projects with the fundamental drivers being made to how premiums are calculated, covers delivered and claims paid. Or to put it another way: might SMCR and GDPR end up capturing the insurance that is fast being left behind, while failing to capture insurance as it is fast becoming? I think there's a real risk of that happening.

## Heading the Wrong Way?

There's also a danger that the compliance and oversight frameworks being introduced for SMCR and GDPR will progressively be seen as irrelevant by the public. This is because the public is putting diminishing weight on what firms are doing, and increasing weight on the outcomes being experienced. So an insurers that ticks all of its boxes for SMCR and GDPR will still struggle to gain public trust if, at the same time, it is doing things in pricing, distribution and claims that produce outcomes that consumers just don't like.

Insurers should not see SMCR and GDPR as 'job done', other than in an essentially legislative sense. Consumers are unconcerned with technical legislation like this, expecting firms to just get on and do that sort of stuff automatically. What they want to experience are the outcomes of a sector focussed on doing things that they find trustworthy. Insurers need to transform not only how they do business, but also how they see and relate to consumers.

## Assessing Integrity

Insurance firms are required under SMCR to have a on-going process for assessing the integrity of their senior executives. That's something that few UK insurers have done before and I fear that a good number will struggle to introduce a meaningful assessment. Most will turn to a supplier of boilerplate assessments, hoping that the Financial Conduct Authority (FCA) will not notice. I doubt if they will, at least for the present, as they will have too much on their hands to grasp this particular nettle. The downside will be that insurers will feel more confident about the integrity of their executives, but with little substantive evidence to back up that confidence. It's an 'Emperor's clothes' risk.

## The FCA's attention to Data

I suspect that the FCA will be waiting for the GDPR to achieve traction within the insurance sector, before returning to address the burgeoning issue of the impacts that artificial intelligence (AI) and data could have on insurance consumers. The danger is that their approach to-date has seemed so half hearted that should they, 'post GDPR implementation', take a more concerted approach to AI and data, the impact on regulator / market relations could be significant. I expect AI and data to become a key testing ground for ethics in insurance.

## Fairness

The whole question of fair outcomes for consumers is in danger of becoming atrophied between GDPR, SMCR and the aforementioned 'wait and see' approach of the FCA to AI and data. Over the next two to three years, something significant will be needed to 'jump start' it again as a core ethics in insurance issue. Whether that comes from the UK Parliament or the UK press is unclear. What is more clear is that price optimisation will be a contributing factor. Insurers that want to take fairness seriously should take their frameworks and stress test them with different varieties of fairness, and with an outcomes perspective. It's as straightforward as that.

## Whistleblowing

It's a year or two since the new rules on whistleblowing were introduced by the FCA. It's likely that they will publish some data on how well firms have been doing and through this, send a big message to the market about what accountability under SMCR really looks like. They could very well publicly hammer home a particular lesson on ethical culture on a firm or individual who has fallen foul of the whistleblowing rules. It will not make pleasant reading.

## Coordinated Critiquing

I foresee more and more attention being given to the insurance sector by a range of organisations looking at artificial intelligence, data and the ethical issues associated with them. This has already happened in the US and will become more of a norm in the UK and other markets. I'm not convinced that the sector has a significantly robust argument to deliver in response, so sparks could fly as the two engage. The great danger is that the sector could rely on a 'you don't understand how insurance works' argument. Let's hope for a more robust, rather than dismissive, response.

## FAT

That coordinating response is likely to be centred around the three FAT principles – fairness, accountability and transparency. Insurers may feel confident of having an answer to all three of those principles, through their work on Treating Customers Fairly, SMCR and GDPR. That apparent strength is however also a weakness. Insurers may have the compliance frameworks in place, but drifted sideways in the ethics of some of the underwriting and claims decisions being made within them. Price, and especially claims, optimisation will be seen as evidence of fine talk not being walked. The danger, if my legal readers will forgive me, is of insurers relying on lawyer scripts for their response to the aforementioned coordinated critiquing. Both sides are clever, but both will struggle to be understood by the other.

## Accountability

The pressures on non-executive directors will grow. As new idea is piled upon new project and uncertain risk and delivery, their oversight will become even more of a challenge. This will lead NEDs to seek new ways of knowing where and when to ask for more, and how to frame the right questions and understand the answers. The problem is that their most obvious source of such guidance are the big advisory firms driving those very changes in the first place. Independent advice will be difficult to come by, but it's needed now more than ever.

## Insurtech

The ranks of 'insurtech' firms seeking to challenge the established markets continue to grow, yet a sense of realism is clearly emerging now. Disruption is not as easy as initially thought and some have had to embrace the failure often said to be part of the innovation process. Yet a paradigm shift does seem to be in the making, primarily through the growing utilisation of various artificial intelligence tools for the automation of decision making. And it is through the AI tools that insurtech firms are promulgating, rather than the newness of the firms themselves, that I foresee most disruption happening. In other words, insurtech firms can often turn out to be rather traditional than they'd like to admit, but it's their new tools that will drive the next generation of insurance.

Artificial intelligence has been around for a long time, but it's adoption is exponential at the moment. And it is in those AI tools that many ethical issues reside. I've covered those issues in several blog posts in recent years, but suffice to say, insurance firms seem reluctant to fully engage on them. I see hints of understanding, but these are invariably stifled by competitive pressures. The end result is limited progress, and the end risk will be a further diminution of trust. I remain surprised that insurers are willing to live with this risk, given PwC's findings in a survey earlier this year:

- 72% of insurance chief executives thought it will be harder to sustain trust in a digitised market
- 28% of insurance chief executives are "extremely concerned" that trust will affect their firm's growth

## Claims Optimisation

The practice of optimising claims settlements has begun in the UK and I think it inevitable that it will become more common. It will lay the seeds of an almighty controversy and could be the ruin of the insurance sector's reputation. Yet those aforementioned competitive pressures, and some clever 'consultancy speak' from data broker suppliers, means that key insurance decision makers may only realise the ramifications of this practice when the damage has already been done. I suspect that the public's attention will be drawn to it during 2018 and the media will recognise that they've been handed a great story on a plate. Insurers need to apply some truly critical thinking to their adoption of claims optimisation and be prepared to justify their end decision. Rather them than me.

## To conclude

To conclude. I foresee 2018 being an eventful year for ethics in insurance. In the shadow of SMCR and GDPR, there are some seismic changes in the making, with significant ethical ramifications. Insurance is a competitive market, and long may it stay so, but it is also a market upon which the public relies, and which the public has to trust. Those bonds are being stretched