# INSURANCE/REINSURANCE

## NAVIGATING INSURTECH REGULATION WITHOUT A MAP

InsurTech—the innovative use of technology in insurance—is leaving the station and pulling the industry forward at a rapid clip. Insurers that don't jump on board soon will find themselves at a distinct competitive disadvantage: According to PwC's *21st CEO Survey*, 85 percent of insurance CEOs believe that the speed of technological change is threatening their company's growth prospects.

A parallel sense of urgency is pushing state insurance regulators, which are legally required to provide a vibrant marketplace for insurers and consumers. Since facilitating technological innovation is part and parcel of this mission, regulators are looking for ways to enable insurers to test InsurTech initiatives that don't clearly fall under existing laws. Forward-looking states are competing with each other for first-mover advantage.

Looking ahead, the challenge for insurers and their tech and financial partners is twofold. In addition to making successful business ventures, they must work with regulators to chart currently uncharted territory. "Companies have to determine if they can win as the regulatory environment takes shape," says Laura Foggan, who heads Crowell & Moring's Insurance/Reinsurance Group. "Constructive dialogue with regulators can only help them get where they want to go."

### HIGH POTENTIAL LEADS TO DEAL FEVER

InsurTech encompasses a host of technological innovations, including Big Data/advanced analytics, artificial intelligence, the Internet of Things, machine learning, blockchain, telematics, software as a service, and more. The industry is actively pursuing all of these, both to address existing issues and to identify new opportunities in a variety of areas: underwriting, product development, distribution, pricing, policy customization, sales and marketing administration, regulatory reporting and compliance, claims processing, customer service, and fraud.

The mounting pace of InsurTech deal activity reflects the industry's excitement about a brighter future as well as expectations that the future is approaching quickly. As Willis Towers Watson reports in its *Quarterly InsurTech Briefing Q3 2018*:

- There were 194 InsurTech transactions in the first three quarters of 2018, the highest such total in any year to date.
- The number of private technology investments made by insurers or reinsurers also hit its highest first-three-quarters level (67 deals) in the same period.

### NO U.S. SANDBOX FOR INSURTECH—YET

One promising approach for regulating InsurTech is a flexible "regulatory sandbox" structure that encourages experimentation while allowing states to oversee and evaluate what companies are trying to do. The "regulatory sandbox" concept proposes a reasonable degree of regulatory flexibility, as exemplified by enforcement safe harbors such as variances, waivers, and no-action letters, combined with continued regulator focus on maintaining consumer protection and risk mitigation.

While regulatory sandboxes for InsurTech innovations have seen widespread acceptance in other jurisdictions—particularly in Asia and Europe—the U.S. lags behind in approval of regulatory sandboxes for insurance. In fact, in some states, regulators have expressed concern that there may be a need for greater oversight arising from the use of new technology by insurers, rather than regulatory flexibility to encourage InsurTech innovation. For instance, New York's Department of Financial Regulation recently issued Insurance Circular Letter No. 1, to advise insurers in New York of their statutory obligations regarding the use of algorithms and predictive models in life insurance underwriting. The department expressed concerns about the potential for negative impact on

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consumers from possible inappropriate use of algorithms and predictive models, while also acknowledging that innovation and the use of technology has the potential to benefit insurers and consumers alike.

Generally, state regulators in the U.S. have noted that increased insurer use of technology may lead to new insurance products, better customer service for consumers, and increased efficiency for insurers, while simultaneously expressing concerns about issues such as data privacy and discriminatory impact or bias in data sets. "It will be interesting to see whether regulatory sandboxes for insurers finally gain traction in 2019 or state regulators find other ways to promote innovation," says Foggan.

## HOW TO NAVIGATE AN EVOLVING REGULATORY REGIME

So the state of play for InsurTech regulation entering 2019 is evolving but as yet officially unchanged. How can industry players navigate a path forward when there's no map?

"The industry and its regulators are on the same side," says Foggan. "Both want InsurTech to succeed, and they know they have to figure it out together. This could help the process move faster and with a solid base of mutual understanding."

The first step is for insurers and tech providers to coordinate their efforts in cooperative ventures that will secure regulatory approval, including through mergers, acquisitions, or joint ventures. Seasoned counsel with experience in technology and intellectual property matters can ease the way for acquisitive insurers, just as insurance-savvy counsel can give tech providers a clear picture of the specific regulatory hurdles that insurers face.

Companies that are developing InsurTech initiatives are advised to meet with their regulators to educate them about the technologies involved. Foggan notes: "Regulators know they need to be educated about the technologies they're being asked to regulate, and they often don't have the staff, budget, or internal expertise to do it themselves. In this context, the potential benefits for both sides are significant. Industry players that can bring regulators up to speed are doing more than improving their own odds of getting a regulatory green light—they're also helping the states get a regulatory jump on other states."

## LLOYD'S OF LONDON: ILLUSTRATION OF AN INSURTECH INCUBATOR

Lloyd's of London, the world's largest market for specialist insurance and reinsurance, has put its own spin on the concept of the InsurTech sandbox.

Lloyd's Lab is a 10-week program in which 10 competitively chosen InsurTech developers work to create solutions for challenges faced by the Lloyd's market in four areas: enhancing the customer experience, building a relationship-driven culture, powering data-driven underwriting, and creating smart insurance products.

Lloyd's is offering a unique opportunity to test new products and ideas, says Mark Meyer, a partner in Crowell & Moring's Insurance/Reinsurance Group and leader of the firm's European insurance practice, but it still has to pass muster with one of the world's most advanced InsurTech regulatory regimes.

"In the UK, insurance is governed by two jurisdictions," notes Meyer, who advises insurers as well as brokers. "First there is the UK via the Financial Conduct Authority (FCA), which recognized InsurTech's potential to transform the insurance business years before its counterparts elsewhere. FCA launched its own InsurTech regulatory sandbox in 2014. There also is the European Union, which is playing catch-up but is working toward setting up its own sandbox."

Meyer cites a synopsis of key insurance policy terms as an example of how InsurTech can help with regulatory compliance. The EU mandates this plain-language synopsis so that policyholders can better understand their coverage. The trick is to automate the production of synopses, which must be customized for each policy. InsurTech's focus on artificial intelligence, machine learning, and advanced analytics can make this process much faster and cheaper as it meets regulatory requirements.

The specter of Brexit also looms large. "While no one yet knows how Brexit will affect insurance regulation in the UK," says Meyer, "the industry is monitoring developments closely and will adjust as needed."