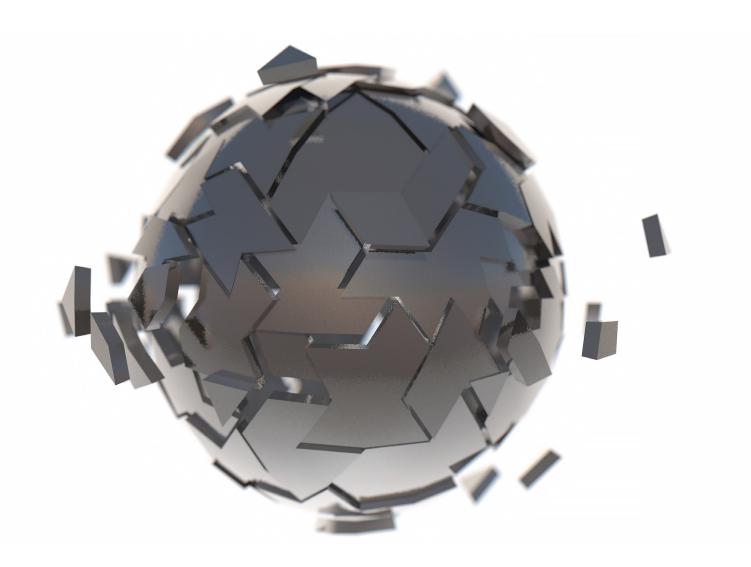
## **Deloitte.**



## **Looking ahead**

The future state of compliance in the insurance sector



Doing more with less in a changing regulatory environment

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## Introduction

In a series of interviews with (Chief) Compliance Officers from Insurance companies the challenges of the compliance function were considered. This article discusses three key investment areas that require attention in order to evolve towards the future compliance function.

Over the last few years, the insurance sector has experienced more than before compliance incidents. As a result, compliance risk management has become a senior management priority. Many insurance companies reported spending a large amount of time and resources on addressing issues and incidents on an ad hoc basis. At the same time, they are facing cost reduction programs that also have an impact on the compliance function.

Insurance companies are looking for a strategic approach to compliance risk in order to improve the efficiency and effectiveness of the compliance function. What are the challenges in the field of compliance? Which developments are driving a necessary change in the compliance function? And how to prepare the compliance function for the future?

In this article, we will dive into these questions. The content is based on market experience and enhanced with the outcome of the compliance function benchmark. This benchmark was performed in 2020 at five large insurance companies in the Netherlands in order to assess the current and upcoming challenges of managing compliance risk in insurance.

#### Compliance function benchmark

#### **Background**

- The Dutch supervisor (DNB) asks insurance companies to substantiate their required capacity for the compliance function and to use the capacity in a risk-based way. Due to cost reduction and an increase in regulation, the compliance function is under pressure.
- Based on the request of Dutch insurance companies, the Compliance Benchmark was developed by the
- Regulatory Risk team of Deloitte Risk Advisory Netherlands (hereafter: "Deloitte").
- This benchmark analyses the design and effectiveness of the compliance function of the Dutch insurers that participated in this benchmark. The outcome of this benchmark provides valuable insights into current market practices.

#### **Approach and Methodology**

- Five large insurance companies (hereafter: "respondents") in the Netherlands have been approached by Deloitte to participate in the benchmark, which all of them did. The results were collected based on a survey.
- An interview with a representative of each respondent was part of the process of collecting the data.

# Which developments are driving a necessary change in the compliance function?

The pressure is mounting on the compliance function of insurance companies, both internally and externally. Increasing regulatory mandates, perpetual talent squeezes, increasing demand for cost reductions, and a growing need for additional capacity for new and emerging risks are challenging them. This view is confirmed by the outcome of the compliance function benchmark.

#### **External pressures**

As regulators themselves are evolving towards a more mature standard, they simultaneously increase the standards for insurance companies. This includes both the regulator's methods and the level of depth of monitoring and supervision on compliance risks. Throughout the sector, we see rising numbers of investigations on noncompliance by regulatory authorities, for instance in the field of (client) integrity, Duty of Care, Solvency II and the effectiveness of the compliance function itself. Compliance functions are trying to keep up with these increasing demands, although they are often struggling to stay ahead of the developments, preventing them to be in charge of their own agenda.

#### Internal challenges

While external pressure is increasing, compliance functions within insurance

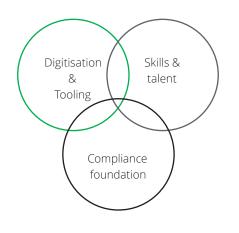
companies are facing internal challenges as well. It is difficult to attract the right people for the compliance function, as this specific type of talent is already scarce. In addition, disparate risk methodologies and inefficient operating models weigh heavily on the capacity of the compliance function. And on top of that, organisation-wide cost reduction programs are current in place at many insurance companies.

#### **Emerging technology**

Emerging technology can be seen as the third driver of change for the compliance function. Regulatory technology (RegTech) has made an entrance. Instances are cognitive compliance, risk sensing and automation/robotics-integrated governance, risk and compliance. The opportunities of big data and analytics, such as increased use of unstructured, high volume data to drive risk

identification and process enhancement and predictive analytics, are considered as key for the compliance function.

### Three investment areas for the compliance function



Based on the compliance function benchmark, we have identified three pillars that are considered as key investment areas for the compliance function: digitisation & tooling, Skills & talent, and the compliance foundation:

#### **Digitisation & tooling**

 Use of data & tooling instead of manual labour, so that resources can be used to achieve strategic goals.

#### Skills & talent

- Compliance professionals are considered true business partners and advisors.
- Re-engineering of traditional resource models and allocation of methods to optimise the use of resources, supported by technology, analytics, managed services, and offshore resources.

#### **Compliance foundation**

 Cost reduction opportunities can be created with efficiencies and effective use of increased capacity across the organisation by means of tools, technology, collaboration with other organisational units (e.g. first line and second line) and resource allocation.

These are discussed in the following chapters.

## Digitisation & tooling: improve efficiency and effectiveness

The compliance function currently struggles with reduced resources and budgets on the one hand, and a steadily increasing pressure to expand compliance capabilities on the other hand. The solution is digitisation of the compliance function. The department gains meaningful new risk instruments when the transition from a static setting to a dynamic trend analysis is completed. It provides them with the tools to make strategic capacity shifts while they are still able to perform deep-dives or extensive analyses.

### The urgency for digitisation and tooling

The external and internal pressures show the urgency for digitisation and tooling. These will help to gain a wider and deeper understanding of the compliance risks that insurance companies are facing.

One of the outcomes of the compliance benchmark is that insurance companies are facing challenges such as data quality and fragmented data sources within the organisation. This happens for instance when a dataset is split and saved in an inconsistent format or location. Before performing data analytics on fragmented data, professionals need to start with a manual transformation of the data, including collecting, checking and repairing (static) data. The estimated effort needed to perform this step is about 80%, which leaves roughly 20% of time and resources to interpret and analyse the data for strategic or regulatory purposes.

By resolving these issues, more capacity will be available within the compliance function to focus on process optimisation and on their role as an advisor for the business. Both the impact of data analytics

and the business strategy should be considered when determining how to reallocate the resources. The next step could be the creation of use cases to provide insight into the (operational) possibilities to use data analytics. For instance, the use of a scan to identify regulatory change. For compliance functions without any data expertise, it is advisable to leverage on the data expertise in- and/or outside the organisation in order to take the right steps towards digitisation.

#### **Centralising data sources**

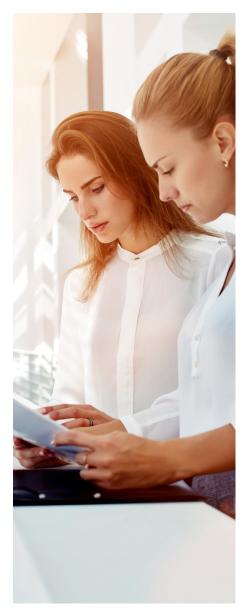
Many insurance companies have started to centralise their data sources and develop data pipelines that enable efficient and effective data gathering. The business should leverage this towards the digitisation of their compliance function. As manual steps are removed from the data transformation process, compliance professionals can focus on performing different types of analytics on the available data. For instance, they could perform a trend analysis to identify integrity risks and predict future risk exposure.

Detecting trends in an early stage allows compliance functions to focus on

prevention instead of on a costly cure. Another benefit is the ability to analyse large amounts of data instead of pulling data samples to estimate a risk. This makes activities such as control monitoring easier and more efficient. For instance, compliance functions could extract data directly from the source data as input for the Systematic Integrity Risk Analysis (SIRA), instead of manually collecting data in Excel. This will save a large amount of time. Also, the risk assessment becomes more objective and can be consulted on a more frequent basis.

## Skills & talent: increased capacity and new competences

The range of skills needed by the compliance function is widening and deepening at the same time. This trend is driven by a continuous increase in laws and regulations that impact the insurance sector, such as the upcoming sustainability regulation. To meet these expanding demands, the compliance function requires a more extensive skill set.



In the past, the focus in a compliance function was on legal or regulatory expertise. Nowadays, there is an increasing need for professionals with a data or technological background or expertise. Simultaneously, many insurers experience internal pressure to cut costs for which the compliance function is certainly not immune. The question is how compliance functions will deal with these contradicting demands.

#### A diverse team of experts

Compliance functions need to effectively utilise their resources to meet the increasing expectations. Next to that, they must identify the skills and expertise currently lacking in their team and attract qualified people to bridge these gaps. Furthermore, diversified training and education for compliance professionals should be encouraged in order to maintain the appropriate knowledge and expertise level. To prevent an escalation of staff costs, compliance functions should look for innovative methods to meet the above-mentioned requirements. For example, introducing tooling and leveraging technology in daily operations will improve efficiency and free up professionals for different tasks. In addition, collaborating with other departments to draw upon their expertise and knowledge (such as technological expertise) should become common practice and a necessity for a well-functioning compliance department.

Building a diverse team of experts will help the compliance department to increase their strategic value to the organisation. There are three approaches that should be considered:

- attracting new employees with the required knowledge and expertise.
- training and educating current employees to expand their skills.
- working closely together with other departments that offer the missing skills and expertise.

However, before selecting one or multiple approaches, the compliance function should first understand its strategic vision and ambition. Only when the vision and ambitions are clear, the function can identify which expertise and knowledge within their department can be increased and what approach would be best.

## Compliance foundation: getting the basics right

In recent years most insurance companies invested in making their compliance frameworks more effective as well as more efficient. However, there are still many opportunities for further improvement, especially the relation between the compliance framework and the broader (operational) risk frameworks. For example, policies and procedures are often not fully linked to risks and controls. In some instances, even risks and controls are not consistently linked.

This results in time and labour intensive monitoring procedures, lack of feedback loops and inconsistencies in risk assessments. Due to these suboptimal conditions, insurance companies have difficulty with identifying priorities, maintaining an (objective) overview of the risk exposure and investigating root causes of issues and their impact on the organisation. Also, identified issues are not adequately monitored until they are resolved. When issues are out of sight, they often continue to grow underneath the surface, with dire consequences when they are not detected in time.

### Building a solid foundation for the compliance framework

In order to future-proof the compliance function, the focus should initially be on building a solid foundation for the compliance framework. Without this foundation, compliance professionals will continue to fight inefficiency and ineffectiveness. By returning to the foundation, the compliance framework can be simplified, and overlaps with (operational) risk frameworks can be resolved.

The next step should be to develop an effective and efficient monitoring and control framework. By linking the compliance framework to the periodic risk assessments, control statements, compliance reporting cycle and issue tracking systems, the compliance function will benefit most from its framework. Embedded feedback loops can help to manage any overlaps with other risk domains.

For those who want to reach an even higher maturity level, connecting the compliance framework to other risk domains should be the goal, as this results in an integrated risk framework. By working closely together with other departments, risk insights will improve while duplication of work is prevented.



## The time to act is now

The modern compliance function requires a more extensive skill set than before. Knowledge of new and emerging risks, data analytics and technological innovations in the business are more important than ever. In light of the challenges the compliance function is facing, the capability to leverage technology for compliance tasks is key. The question is how compliance functions will meet these requirements.

For every organisation it will differ what the areas for improvement are and what a suitable approach is in making the Compliance function "future proof". It will depend amongst others on the maturity of the Compliance function and the (technical) capabilities within the organisation. For example, the following areas can be taken into account:

- Minimise manual labour in control monitoring, risk assessments and compliance reporting. This will make it easier to prioritise and focus on strategic matters.
- Develop a learning curriculum to expand the current skill sets of the compliance professionals and create an all-round team.
- Clearly define the scope of regulations for which the compliance function is responsible. Otherwise, the function could become a collecting bin for topics to which the word "compliance" is attached.
- For digitisation to be effective, the data quality issues need to be resolved and centralised data sources must be created.
- To conclude, the compliance function can reinvent itself by investing in diversifying the function with the right people, and by supporting this with adequate processes combined with new technologies. Then it will become a valued strategic partner to senior management with a clear vision. However, the time to start investing in the future of compliance is now.



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