



# KPMG's Regulatory Update

The Bermuda Monetary Authority (BMA or the Authority) continues to strengthen the regulatory landscape of the jurisdiction. KPMG's Regulatory Update provides a recap of the BMA's developments, from October 2018 to March 2019, and our commentary of the impacts on Bermuda's financial services sector. Areas include:

1. Insurance and Reinsurance
2. Cyber
3. Banking and Asset Management
4. Fintech; and
5. Anti-Money Laundering (AML)/  
Anti-Terrorist Financing (ATF).

We would welcome the opportunity to review these or any other business issues with you.

We are currently reviewing the 2019 BMA Business Plan and we will provide our review and commentary shortly.

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## Insurance and reinsurance

### **2018 year-end BSCR filing requirements**

The 2018 year-end filing requirements for Insurers were released by the BMA in December along with the BSCR templates for the year. The filing deadline is 30 April 2019. For more information on each class, please click on the links below.

- [Class 3A](#)
- [Class 4 and Class 3B](#)
- [Class D and Class C](#)
- [Class E](#)
- [Insurance Groups](#)

A new BSCR calculation came into force on 1 January 2019.

### **What's the impact?**

There is a transition period in place to shift BSCR capital requirements from the 2018 year-end filing requirements to the new ones applicable from 1 January 2019. For general business (classes 3A, 3B and 4), capital requirements will transition linearly over three years. For long-term business (classes C, D and E), capital requirements will transition linearly over 10 years.

The key changes to the BSCR calculation are:

- Mandatory use of a look-through approach for assets.
- Significant increases in the capital charges for some types of equity. For example, charge for listed equity securities in developed markets has increased from 14.4% to 35%.

- Significant increase in operational risk charge especially for higher-risk insurers.
- Increases in the credit risk charge, likely more material for P&C business.
- Increases in the exposure base for P&C premium risk.
- Lower diversification between the major risk categories: insurance, market and credit.
- Changes in diversification within underlying risk modules (e.g., equity risk, P&C reserve risk).

KPMG can help you with your BSCR filing requirements including the FCR, CISSA reports.

## Catastrophe risk in Bermuda - BSCR stress testing and modelling practice analysis

The BMA released its third annual [Catastrophe Risk in Bermuda Report](#) in December 2018. The annual report gives a high-level overview of the catastrophe risk stress testing and modelling practices in Bermuda. Highlights from the report include:

- Compared to the previous year, net catastrophe exposure slightly decreased by about 2%.
- The (re)insurers have increased their statutory capital and surplus by 12%.
- The overall industry's resilience to potential catastrophe events has further strengthened compared to last year.
- The global share of gross estimated potential loss assumed increased by about 2%.
- The report also reviewed cyber risk stress testing and the analysis shows that the (re)insurers' own defined worst impacts from cyber risk would have a minimal effect on their statutory capital.

## What's the impact?

The BMA's annual report is essential in providing Bermuda insurers and other stakeholders, locally and globally, with insights into catastrophe risk within the local market. Overall, the results of the report highlights the industry's resilience to major, but improbable, catastrophe events, as well as the sophistication and advancement of the modelling practices in Bermuda. This emphasised the reputation of Bermuda insurers as being generally well capitalised and technically proficient.

## Insurance managers annual return

On 27 February 2019, the BMA issued new templates for Insurance Managers, Brokers and Agents annual return with supplementary rules for completing the return. The first filing of the revised template is due on or before 30 June 2019.

## What's the impact?

Insurance Managers, Brokers and Agents will now be required to complete additional schedules in the annual return filing. They include questions on Cyber Risk Management, Anti-Money

Laundering and Anti-Terrorist Financing Risks and Controls, Corporate Governance and Sanctions, and the BMA will expect this additional information or for licensed entities to have it readily available in order to be able to answer positively to these questions.

## Alternative capital report 2018

The BMA released its first annual [Alternative Capital Report in December 2018](#). The Authority, in 2017, introduced an enhanced reporting requirement for (re)insurers with alternative capital structures in order to facilitate collection of key data, such as structure of the insurer and summary of contract details. This enhancement is essential in maintaining an effective supervisory regime for this rapidly growing and evolving sector. Additional highlights include:

- Aggregate exposure of non-life (re)insurers backed by alternative capital was approximately \$51.9B at year-end 2017.
- Gross written premiums for the period was \$3.9B.
- Assumed risks were split across nine lines of business covering four major geographical regions (United States, Europe, United Kingdom, and Asia).
- Property catastrophe (including property retrocession) was the biggest line of business written, representing approximately 94% of GWP while the United States was the largest risk region, representing 40% of aggregate limits covered.

## What's the impact?

The BMA's report provides promising insight that there has been a steady growth of alternative capital within the Bermuda insurance market. This is despite the 2017 losses from hurricanes Harvey, Irma, and Maria. Bermuda continues to be a quality jurisdiction for insurance risk securitisation, and the Authority will use information from the Alternative Capital Schedules and Statutory Financial Returns to provide insights to the industry.

## Bermuda insurance-linked securities (ILS) market report – December 2018

The BMA issued the Bermuda [ILS Market report](#) in December 2018. It provides an overview of the market, both the primary and secondary markets. The report highlights that Bermuda remains the leading domicile for the issuance of ILS and also other forms of capital markets backed reinsurance, underscored by the fact that 74.2% (according to the BMA's figures) of total outstanding ILS capacity was issued here at the end of the period. Additional highlights, include:

- Since 2010, 210 Bermuda-based Special Purpose Insurers (SPIs) have been registered and there have been 243 Bermuda domiciled ILS deals issued.
- Bermuda is also host to foreign ILS listings on the Bermuda Stock Exchange (BSX) which increases the depth of the secondary market.
- 91 ILS are listed on the BSX with an aggregate nominal value of \$24.1B.

- Eight new ILS deals totalling \$2B were listed on the BSX during the quarter, while seven deals in the amount of \$1.1B matured.
- Bermuda-based SPIs accounted for all catastrophe bond issuances in Q3 2018.

### **What's the impact?**

The analysis by the BMA clearly demonstrates Bermuda's position remains as the domicile of choice for the issuance of ILS transactions, and as the country continues to reaffirm its reputation as a quality jurisdiction, the ILS market will also continue to grow.

### **Captive report 2018**

The BMA released [Captive Report](#) in December 2018. It highlights the results from statutory financial returns submitted through the Authority's Electronic Statutory Financial Return (E-SFR) system as of 31 October 2018. The report provides highlights of the captive industry, including:

- Business written by geographical region, lines of business, and industry of parent company.
- Industry utilisation of Bermuda captives, their premium shares, and the industry profile of the market.
- Balance sheet composition by asset, liabilities, and investment allocation.
- Profitability indicators.

### **What's the impact?**

The BMA's report is an excellent example of the benefits that are gained through the use of electronic filing and data analytics enabling the Authority to produce quality reporting for the industry. The report can be referenced by the market for benchmarking purposes, as well as provide prospective organisations with useful information to consider when locating to Bermuda. The jurisdiction continues to be home to captives servicing a broad range of industries.

## Cyber

### **Cyber report – December 2018**

The BMA included questions in the 2017 year-end Bermuda Solvency and Capital Return (BSCR) filing designed to assess information security, cybersecurity, and data privacy preparedness of (re)insurers. The Authority has used this information to produce the 2018 Cyber Report which was released in December 2018. It provides feedback on the information obtained in 2017 year-end filing and provides context for the 2018 year-end information requests from insurance managers, agents, brokers and the BSCR, as the BMA has enhanced the 2018 filing requirements. The report also shares a summary of the market data and the risks obtained from the information.

This Cyber Report follows on the noticed published on 12 February 2018. The notice outlined some expectations of licensed entities regarding the management and reporting of cyber security risks and incidents. In that notice, the Authority stated: "As with any material risk, all licensed undertakings are required to have robust policies, procedures and controls in place to identify, assess and manage cyber security risks on an on-going basis consistent with the prudent business minimum licensing criterion."

It is apparent from the information provided in the 2017 BSCR cyber resiliency questionnaire and feedback that technology risk awareness and cyber security in particular has grown. Most (re)insurers have made efforts to enhance technology. However, there is still a lot of work that needs to be done before the BMA can achieve a level of assurance that the risks are effectively mitigated.

### **Cyber underwriting**

According to data captured in the 2017 BSCR 37 Bermuda Commercial Insurers and 15 Groups indicated that they are writing affirmative (direct) cyber insurance. As 2017 was the first year of reporting, there was variances in terms of interpretation of what is required. Enhancements and additional guidance has been included in the cyber risk reporting requirements for 2018 year-end CSR filings. The BMA expects both affirmative and silent (indirect) cyber risk, (re)insurers need to have the relevant skills, clear strategies, and Board-approved risk appetites.

### **Cyber stress scenarios**

Commercial Insurers were required to provide cyber risk coverage data in the BSCR, including estimated aggregate exposure, and own cyber risk worst-case annual aggregate loss scenarios, and the underlying assumptions. The data showed that Commercial Insurers' own worst-case scenarios from affirmative cyber risk coverage would not have significant impact on their statutory capital and surplus. The average gross and net impacts were 5% and 4% respectively. The BMA's general view is that much larger losses could arise from silent cyber contracts.

### **What's the impact?**

The cyber information request has been enhanced in the 2018 filing to include all financial services sector players in Bermuda, including Insurance Managers, Agents, Brokers and the BSCR which will provide broader market information and allow the BMA to perform thematic assessment of the technology risk posture of licensed entities.

With specific emphasis on the BSCR submissions, recurring questions have been asked by our clients. Some examples include:

- Does the cyber risk charge effect the Capital charge by the company and;
- If schedule Class E Schedule V (e) returns of BSCR template have a weighting difference for yes/no questions answered and how does this flow through to a capital charge effect for the company.

There is not a weighting per yes/no answer in Section A – Business summary questions and Section B – NIST Control summary for Class E Schedule V (e) returns that directly flow through to the Capital charges. However, these answers would indirectly effect the operational risk scoring charge covering the category of “Information systems” (“IS”).

IS assessment category effects the operational risk score for separate scoring in the BSCR return compilation tabs:

- Risk identification;
- Measurement;
- Response; and
- Monitoring and reporting.

All of the above directly link to a capital charge in the BSCR return through the Operational risk charge calculation.

Schedule V (e) also talks directly to Governance, Risk and Controls (“GRC”) and a view of assessing effectiveness of GRC around IS and these would need to be assessed as part of the IS category in each relevant operational risk score area above.

Operational risk charges will increase for insurers, especially those with mid-to high-risk profiles. For high-risk profiles, the increase can be up to 10%. For low-risk profiles, the increase is smaller at around 1%-2%.

# Banking and Asset Management

## **Managing third party risk through new outsourcing guidance**

The BMA issued a [consultation paper](#) on the 5 November 2018 setting out new outsourcing guidance for Relevant Licensed Entities (RLE), which are defined as any Bank, Credit Union, Trust Company, Corporate Service Provider, Money Service Business, Investment Business, Fund Administrator, and the Bermuda Stock Exchange.

Responses to the consultation paper were due to be submitted to the BMA by the 4 January 2019. The new guidance replaces existing guidance on outsourcing for Banks and Deposit Companies published in May 2017, and is in response to the Authority seeing an increase in the use of outsourcing by RLEs in Bermuda over the last three years.

The guidance requires in scope companies to identify material outsourcing arrangements and for those deemed material, a comprehensive submission of compliance must be made to the BMA by the 30 August 2019. The alternative option is for the CEO to formally attest in writing that the existing material outsourcing identified complies with this new guidance. These attestations are to reach the Authority no later than 23 December 2019.

## **What’s the impact?**

KPMG anticipates the BMA to produce a stakeholder letter to address comments provided during the consultation stage. If changes are to be made, the BMA will do so before issuing the final guidance paper and we expect the final guidance to be issued later in Q1/Q2 2019. The new guidance, once finalised will place a significant burden on organisations to meet compliance in advance of the proposed implementation date on 1 January 2020.

The introduction of this new guidance on outsourcing will require all organisations to review whether any existing outsourcings are material or not and if deemed so, then a submission must be made to the BMA. The submission is onerous and will require organisations to conduct a comprehensive assessment of their outsourcing arrangements, policies, procedures and internal controls in order to complete the submission and/or produce a formalised compliance attestation to the BMA. KPMG is monitoring the BMA’s progress and more information on how we can help can be found [here](#).

## **Banking Digest**

The BMA issued the [Banking Digest publication](#) in November 2018. The publication provides an overview of the Banking industry including; Basel III Requirements, a summary of selected indicators such as capital, earnings and asset quality for the period, and market analysis.

The Digest also provides an overview of important publications issued during the last quarter by international organisations and national supervisory authorities such as the Banking Committee on Banking Supervision, Bank of England and the Financial Conduct Authority.

Performance highlights for the period included:

- The banking sector’s capital position remained sound during the period, with the CET 1 Ratio and Risk-Asset Ratio (RAR) increasing to 23.1% and 21.5%, respectively.
- The leverage position was marginally higher at 8.4%.
- The banking sector’s assets fell by 1.3% to \$21.6B over the past year, primarily driven by declines in loans and advances and investments.
- Interbank deposits were higher, up 12.7% over the same period.
- Bank performance improved over the past year, as banks posted a significant increase in net profits compared to a year ago; improving overall returns.

## **What’s the impact?**

The publication is for information purposes only, but overall provides useful insights into the Banking sector. The publication is issued on a quarterly basis.

## **Bermuda's Coordinated Portfolio Investment Survey (CPIS)**

The CPI [report](#) is produced as part of the IMF's comprehensive international survey and measures Bermuda's holdings of foreign portfolio investment assets. Foreign portfolio investment assets relate to tradable financial instruments, other than direct investments or reserve assets, issued by unrelated non-residents. Overall, the aim of the CPIS is to improve the statistics of holdings across the globe of portfolio investment assets in the form of equity, long-term debt and short-term debt. The report covers Bermuda's CPIS results for 2017.

### **What's the impact?**

Bermuda's participation in the CPIS contributes to improved understanding of Bermuda as an International Financial Center and its impact on global financial inter-mediation. Overall, the information provided in the report was positive and ultimately enhances the reputation of Bermuda and re-emphasises Bermuda's commitment to a high standard of transparency.

## Fintech

### **Digital asset custody code of practice**

The BMA released a draft Code of Practice for Digital Asset Custody (the Code) for consultation that prescribes measures to ensure a high level of care when safeguarding clients' assets. The Digital Asset Business Act 2018 makes provision for Digital Asset Business licenses and gives power to the Authority to issue Codes of Practice to ensure the business is conducted in a prudent manner. The Code published seeks to protect the public and to clarify the Authority's expectations in terms of the custody of digital assets. The Code is a detailed document covering both technology and business controls in specific areas like hot and cold storage, key generation, transaction handling, incident reporting, and more. Comments on the draft Code were due for submission to the Authority on 18 January 2019.

### **What's the impact?**

The Code is complementary to the Digital Asset Business Act and Regulations and highlights the quality of the work done by the BMA to build on cyber security acumen, as they continue to move to become regulatory leaders in digital assets. KPMG anticipates the BMA to produce a stakeholder letter to address comments provided during the consultation stage. If changes are to be made, the BMA will do so before issuing the final guidance paper.

Craig Swan, Managing Director, Supervision (Insurance) at the Authority further explained: "This technical publication highlights the quality of the work done by our team at the BMA to build on our cyber security acumen as we move to become regulatory leaders in digital assets. It is aligned with the BMA's 2018 Business Plan objectives of being proactive, comprehensive and forward-looking."

## Anti-Money Laundering (AML)/Anti-Terrorist Financing (ATF).

### **AML-ATF Sectorial Guidance Notes for CSPs**

On 3 October 2018, the BMA issued sector specific AML/ATF [guidance notes](#) for Corporate Service Provider Business ("CSPs").

### **What's the impact?**

The BMA has provided guidance on the term used in the business context by CSPs as 'Customer' and the 'Beneficial Owner of a customer', where a term used as a 'Customer' can be a private individual, legal person, trust or other legal arrangements can be termed as a customer of CSPs seeking services or business product offered.

The term 'Beneficial Owner of a customer' can be used for any persons, whether private individuals, legal persons or any arrangements, that effectively own or controls more than 10% of customer's funds, assets or voting rights or in the case of trusts or similar legal arrangements.

### **Notices and interpretative notes**

The BMA has issued a few notices and interpretative notes during the quarter to assist regulated financial institutions:

1. On 6 December 2018, the BMA issued as part of the Bermuda Solvency Capital Requirement an AML and Suspicious activities reporting requirement for the 31 December 2018 submission. [Bermuda Solvency Capital Requirement](#);
2. On 6 December 2018, the BMA issued a notice to Industry on AML/ATF Regulated Activities, the [interpretative note](#) includes the following:
  - The definition of "AML/ATF regulated financial institution" under the Proceeds of Crime Act 1997 has been amended to include institutions which carry out any of those activities as set out in the FATF recommendations.
  - Most of the activities which have been added to the definition are covered by legislation. However, during the CFATF assessment of the Bermuda's AML/ATF regime, NAMLC determined that entities carrying on lending, financial guarantees and financial leasing business, other than by a regulated financial institution, were not subject to regulation under the proceeds of crime legislation.

To address this gap, the following amendment was made as set out in the new Schedule 3:

- a. Underwriting and placement of life insurance and other investment related insurance; and
- b. Money and currency changing.
- The Authority also clarifies the interpretation and application of the following activities:
  - o *Individual and collective portfolio management (Paragraph (i)).*
  - o *Underwriting and placement of life business and other related investment related insurance (Paragraph (II)).*

## **Consultation Paper on Proposed Legislative Amendments to AML Legislation – NAMLC**

The [consultation paper](#) was submitted to industry in November 2018. It seeks feedback on the Government's intention to further update its Anti-Money Laundering/ Anti-Terrorist Financing (AML/ATF) framework.

Key amendments proposed:

- extend existing disciplinary measures/penalties, which can be imposed by supervisors on their supervised entities, to be available for breaches of obligations in relation to international sanctions;
- enlarge the list of entities in respect of which a decision to impose a disciplinary measure/penalty can be published to include real estate brokers and agents;
- permit the publication of any enforcement action taken by the supervisory authorities; and
- clarify that the Financial Intelligence Agency's (FIA) power to make disclosures to the Governor to facilitate the discharge of his statutory functions in relation to international sanctions, will also extend to the authority to whom the Governor may extend any of those functions.

With the approval of Cabinet it is hoped that the finalised Bill will be tabled in Parliament during 2019.

## **What's the impact?**

Extending the scope of the regulatory reach and the proposed amendments support Bermuda's continued efforts to enhance the effectiveness and technical compliance with international standards. NAMLC aims to fill gaps in the legislation which have been identified by the Mutual Evaluation process.

# Additional regulatory areas

## **BMA regulatory update**

The BMA published a [regulatory update](#) for the financial services sector on a quarterly basis. The BMA released their regulatory update in December 2018 for the July – September 2018 period. The update reports on activities at the BMA and developments impacting the financial sector, as well as the community, including: regular statistical data covering Bermuda Dollar money supply, Bermuda banks' balance sheet analysis, and other financial and company sector information updated for the quarter ended 30 September 2018.

## **Global Financial Innovation Network (GFIN)**

The BMA announced on 31 January 2019 that it has joined the Global Financial Innovation Network (GFIN), a group of 29 international organisations committed to supporting financial innovation in the interests of consumers. GFIN seeks to provide an efficient way for innovative firms to interact with regulators, including a cross-border pilot for firms wishing to test innovative products, services or business models across more than one jurisdiction. It also provides a forum for joint Regulatory Technology (RegTech) work and collaborative knowledge sharing.

# Contact

We welcome the opportunity to discuss with you how these updates may impact your business. Please reach out to your KPMG contact or me.



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