



Innovative risk approaches

New compliance and conduct solutions

Claims transformation

One of a series of seven insightful and instructive articles that examine a set of interconnected themes and trends that are expected to drive the traditional claims function into a new future of customer-centric, digitally-enabled, value-driven service and efficiency.

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Client preferences and experiences should be at the core of every insurer's business and supported by a clear set of values that organizations — and their suppliers — live by every day. In today's fiercely competitive environment, achieving a strong and trusted reputation will go far in attracting and retaining business while avoiding unwanted regulatory attention. Today's industry has reached a point at which it must enhance client and regulatory trust. A new approach to reducing and managing conduct risk is in order. Risk and compliance is one of the seven forces that are transforming the claims function and is explored further in this article.

Conduct risk is broadly defined as any action by a financial institution or individual that leads to client detriment or an adverse impact on market stability or competition. The conduct of insurers and the wider financial services industry has, of course, faced increasing scrutiny in the wake of the shockwaves caused by the 2009 global financial crisis and more recently on insurers' response to pandemic related claims.

These events force regulators and policy makers to take action to address these issues. In the UK, for example, the Financial Services Authority (FSA) was split into the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) in 2013 to build financial stability in the UK financial system and address conduct by protecting clients, market integrity and promote competition. There has also been an increase in the development and introduction of regulations and policies such as Solvency II, the Enterprise Act, Insurance Distribution Directive, Renewal Transparency, Operational Resilience, and Senior Managers and Certification Regime, to name a few.

Unfortunately, many claims organizations today, are still reacting to compliance and conduct issues *after* they arise or are prompted by regulatory scrutiny. Recently, insurers' conduct has been questioned through the FCA's Business Interruption (BI) test case¹, pricing review² and the FCA consultation paper on a Consumer Duty³, with similar initiatives being taken in other global markets such as the US and Australia.

Trust in the market is at an all-time low and the UK's BI test case and Consumer Duty consultation paper highlights the importance of aligning robust controls and capabilities to assess coverage and a client centric culture. And as insurance products evolve to cover intangible risks, this will become more important. Clients and brokers alike will demand improved certainty around policy wording and coverage so that there is full transparency on what is and is not covered.

Data and analytics could help manage future risks and costs

Traditional models that many claims organizations have today, invest significant resources to monitor and manage risk, conduct and compliance. But these models are under increasing scrutiny and future best practices should look

quite different. Risk and compliance teams that embed data specialists and modern processes could set the gold standard, delivering optimized risk and compliance management. For example, many claims organizations have faced challenges in identifying complaints in-line with the FCA definition of a complaint. Some businesses have smartly embraced speech-to-text analytics technology. Embracing and investing in digital and data solutions of this sort can help build a holistic and integrated model that better supports effective risk management.

In this model, the heavy lifting across the entire claims value chain, both internally and across the supplier network will be completed through real-time data analytics that eliminates costly, time-consuming manual processes. Machine learning will support the identification of emerging business risks and prompt remedial action or new processes before any damage is done.

With today's increased regulatory — and environmental — standards and reporting, it is imperative that claims organizations invest in the right risk-operating model, harnessing data use to help increase process efficiency and reduce operating costs.

Risk management demands a deeper understanding of business processes

Transparency and rock-solid business processes are as important to today's claims organizations as capital allocation and liquidity. Systemic claims or risk-management failings, or regulatory breaches, can produce severe consequences, including the suspension of an insurer's authorization to write new business. For example, the Danish Financial Supervisory Authority ordered an insurer to stop writing new business due to solvency capital requirements.⁴

Insurers developing a deeper knowledge of their business processes will also be in the best position to meet today's ever-evolving expectations and needs. For example, economic volatility has a significant influence on claims costs — recall the recent changes to the discount rate applied to claims for future loss in the UK. This had a significant impact on reserve holdings and reinsurance costs. With economic volatility likely to continue, claims functions will need robust processes to assess such risks.

¹ <https://www.fca.org.uk/news/press-releases/supreme-court-judgment-business-interruption-insurance-test-case>

² <https://www.fca.org.uk/news/press-releases/fca-sets-out-proposals-tackle-concerns-about-general-insurance-pricing>

³ <https://www.fca.org.uk/publications/consultation-papers/cp21-13-new-consumer-duty>

⁴ <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/danish-insurer-gefion-appeals-regulator-s-order-to-stop-writing-business-57786845>

As artificial intelligence and algorithm-based decision making continue to emerge, understanding how decisions are calculated will also be heavily scrutinized. Claims organizations need to consider establishing models that are consistently ethical, and that specific groups are not discriminated against, while maintaining a robust vetting of decisions. Protection of vulnerable or disadvantaged clients and customers is high on the agenda of many regulators and governing bodies around the world. Insurers need to respond accordingly.

In Australia, for example, Part 9 and 10 of the *2020 General Insurance Code of Practice*⁵, which came into force 1 July 2021, commits code subscribers to take extra care with vulnerable customers and those experiencing financial hardship. In the Netherlands, the Dutch Association of Insurers (DAI) introduced the *Ethical Framework for the application of AI in the Insurance Sector*⁶ and made it binding on DAI members as of 1 January 2021. Ensuring that AI decision making does not prejudice certain customers will be key.

In this environment, detailed knowledge of internal processes, thorough training and cultural alignment across the enterprise, will be instrumental to claims and risk management functions that will effectively prevent these issues from arising.

Foster collaboration and accountability to align suppliers

Claims organizations continue to hold regulatory responsibility — and reputational risk — for the actions of their suppliers and third-party networks. We expect to see supplier panels becoming more community-based in some contexts and utilizing the gig-economy model to enhance local service to clients. There are many advantages to this, but also challenges.

In particular, overseeing supplier service delivery could become increasingly difficult amid the widening array of suppliers in play today. As we note in our related claims article — [Agile claims supply chains: Building an ecosystem of strategic partners](#) — insurers are wisely charting a new path as claims teams focus on transforming supply chains to enhance overall agility, transparency and efficiency.

Once claims organizations have clear processes in place that articulate how each supplier will provide services and adhere to all regulations. This along with a comprehensive set of service metrics and performance targets should also be in place. Monitoring of third-party performance and regulatory compliance in a robust, seamless and integrated way will be key to managing reputational and business risk.

Approaching supplier management with such a clearly defined and collaborative approach greatly increases the

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prospects for success in today’s competitive environment. Suppliers should be treated as an extension of the claims function — holding the same values and service priorities, including fair treatment of clients.

Aligning client experience, conduct and cultures to risk and compliance will be a differentiator

As regulatory expectations evolve and scrutiny grows, aligning client experience, conduct and culture, and risk and compliance, needs to be a priority for executives and senior leadership. It requires investment, resources and a commitment to building the right culture in order to avoid reputation damage and financial penalties. In the UK, for example, the FCA imposed fines worth GBP224 million — equivalent to USD308.8 million — for conduct-related issues in 2019/20, averaging GBP18 million (USD24.8 million) per firm.⁷

The FCA consultation paper on Consumer Duty highlights how these levers need to be aligned. Firms will be required to consider what outcomes consumers could expect from their product or service and enable rather than hinder the delivery of these outcomes. This would require a significant cultural shift from what we see in many claims’ organizations presently.⁸

Culture and organization-wide buy-in are critical. Without this, reactive solutions that don’t address underlying issues are likely to be the result. Understanding how employees view compliance and conduct can drive progress in providing the clarity needed to achieve the target state.

Employees form a significant part of the claims journey and impact the client experience, compliance issues and conduct risks. Providing continuous mechanisms for claims teams to deliver insights into the development of the business will ensure that the right culture is hardwired to embrace risk management and compliance. This benefits management too — an understanding of what employees are experiencing and thinking enables better-informed decision making at the top. We explore the workforce of the future further in [Creating a modern claims workforce: Meeting a bold new era of challenges](#).

⁵ <https://insurancecode.org.au/resources/2020-general-insurance-code-of-practice/>

⁶ <https://www.verzekeraars.nl/media/8220/dutch-association-of-insurers-ethical-framework-on-ai-in-the-insurance-sector.pdf>

⁷ <https://www.ft.com/content/1a465da6-21d6-46b3-8747-b145cb797466>

⁸ <https://www.fca.org.uk/publications/consultation-papers/cp21-13-new-consumer-duty>

Another important cultural enabler involves recognizing employees who have actively challenged the status quo to improve client or regulatory outcomes. Celebrating such successes will enhance employee morale and engagement and underline the fact that client and conduct issues are always genuinely taken seriously by the business.

Strong whistleblowing policies that encourage employees to raise issues are also important. This can also enhance collaboration across the three lines of defense — front line, risk management and internal/external audit.

Often, we see disjointed approaches taken to risk and compliance from one department to another within claims organizations. It is vital that everyone is part of the same journey with the same level of commitment to the effective management of risk and compliance. Incorporating it into the wider claims strategy will support this and ensure that departmental or functional blockers are minimized.

Insurers need to look beyond ensuring compliance with current regulations and strive to embed holistic, innovative approaches that sustain a strong, progressive risk culture.

Transforming risk, conduct and compliance for the future

Embracing and investing in digital and data solutions can help build a holistic and integrated model that better supports effective risk management. Insurers should consider the following to build a risk and compliance function of the future:

- 1 Collaborate to develop your claims strategy and structure.** Ensure your approach is mutually aligned, accepted and embodied across all three lines of defense. Discuss, debate and review the present state and desired future state. Be open to new ideas. By investing now, you should see the benefits long into the future.
- 2 Make compliance and conduct part of continuous-improvement programs.** As new processes are developed, they should deliver positive client outcomes, while minimizing reputational and operational risk and regulatory compliance exposures. Vulnerable clients are likely to be a key focus area for regulators and insurers need to ensure adequate steps are taken to protect them.
- 3 Embrace compliance and conduct across the claims organization.** Provide your risk function with a platform to influence strategic and business planning. Empower claims to oversee and govern the first line's adherence to their risk responsibilities. Ensure that all suppliers are closely aligned with all values and practices with your oversight and management being data-led.
- 4 Embed data and analytics and emerging technologies.** Explore how automating standardized and transactional risk processes can free capacity and increase employee activities that enhance risk-management capabilities. Apply forward-looking, digitally-driven risk techniques and tools to improve analysis and proactive identification of mitigation opportunities. Data and analytics will do the heavy analysis and the risk team will manage remedial action by exception.
- 5 Ensure appropriate experience and capabilities in risk and compliance teams.** This is important not only to deliver current requirements but also to ensure you're ready for emerging risks and evolving regulations. Coupled with robust succession planning, build your internal capability through training and tailored development plans.

Explore our [Claims Transformation](#) articles series further to learn how the seven forces are affecting the claims function. If you'd like to discuss how KPMG professional can help your organization with its claims transformation journey, please contact us.

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