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HOT TOPIC BRIEFING – 'INSURTECH'

The insurance industry is often regarded as being less proactive than the banking industry in leveraging new technology, but many participants have long embraced technology and the use of "big data" in systems and processes. What the industry has not seen a great deal of yet is the much hyped disruptor businesses.

That said 2016 saw a noticeable increase in investment by (re)insurers and third parties in insurtech projects. Technology that was once considered science fiction is fast becoming reality, from driverless cars to medical robots, but innovation can expose new legal and ethical issues which have implications for regulators, manufacturers, distributors and users of this technology.

This briefing takes a high-level look at some of the issues affecting the rapidly evolving world of insurtech.

Why invest?

The threat of disruptive technology and its potential to revolutionise the insurance industry is perhaps overstated by some parts of the media, but excitement surrounding technology like blockchain is attracting huge interest from government, regulators, (re)insurers and investors.

One of the many attractions of investing in technology is that it can be quickly scaled and readily adapted for multiple purposes. Third parties are drawn to investing in start-ups developing innovative financial services technology to sell to insurers (and ideally other financial services companies), which avoids the complexities and constraints of owning a company that operates in a highly regulated environment. (Re)insurers themselves are also investors in insurtech and the soft reinsurance markets and low interest rate environment mean they need to get the most out of their investment. (Re)insurers investing in insurtech can potentially benefit from both the creation of demand for new insurance products that support the adoption of new technology and the generation of additional revenue from licensing intellectual property to other insurers or financial services companies.

The benefits of collaboration

It may be attractive to some (re)insurers to adopt a 'wait and see' strategy when it comes to insurtech, but those who are not part of the development process risk losing out on exclusive arrangements with technology companies or new distribution networks and critically, in having access to intellectual property in new technology. Clearly those with deep pockets are in an enviable position to acquire, or link-up with the most innovative companies and we have already seen a number of partnering arrangements between large insurance groups and start up businesses (Ageas and Back me Up, White Mountains and Buzz Move and Aviva and Luther Systems, to name but three).

A complementary approach involves collaboration between the insurance industry and other financial services industries looking to adopt similar technology. Again, there are already examples of joint projects across industries. Closer collaboration on common interest projects such as blockchain could speed-up their development (even though the use cases for blockchain may be different across industries).

"Insurtech", as a concept, is a broad church and includes:

- The use of data from a variety of sources to enable insurers to price risks more accurately and on a basis which is more personal to the insured.
- The use of telematics, smart home or wearable technology to monitor driving, home use and lifestyle behaviours respectively to underwrite and engage with the customer more effectively
- Development of mobile apps with a view to building, launching and monitoring new products or enhancing existing ones
- The use of technology such as blockchain, to improve underwriting and claims processes

Collaboration however raises issues in particular around the protection of intellectual property, but there is a precedent that participants could look to, to help. The telecoms sector has worked for many years with common platforms based on an open membership model, where all who join agree to make their intellectual property available at fair, reasonable and non-discriminatory rates to all other members. This is how standards like GSM, 3G and 4G conquered the world and provided a base level of common technology for everyone to build their differentiating products on, whilst ensuring that intellectual property developed by individual companies remains protected and is paid for by everyone who uses it (unless the owner chooses to make it available for free). Participants in fintech/insurtech projects could learn from and adapt such a model for their own purpose for mutual benefit.

Legal and regulatory challenges

There is always potential for legal and regulatory issues to arise when new technology is introduced to a market. From a regulator's point of view, technology can improve the take-up of financial services products by customers but it presents new risks, in particular around the use and security of customer data where health and lifestyle information is being collected and analysed, or where personal information is used by insurers derived from third parties (e.g. social networks; online retailers; smartphone operators). Questions have already been asked by a number of regulators about the implications for consumers of developments in technology and artificial intelligence is raising ethical issues that will become more complex and difficult to respond to as the technology develops.

The mainstream adoption of radical technology by the industry will depend on the law and the ability of regulators and (re)insurers to respond to new risks. The industry will need to openly engage with regulators and bring them on board in parallel in order to influence the development of regulation that will not stifle innovation. In the UK, the FCA, PRA and the UK Government is officially supporting the development of new technology and the use of 'Big Data', but the FCA in particular remains acutely aware of its obligations to protect consumers and ensure the safety and soundness of the insurance market.

The challenges for businesses will be in ensuring that they can act quickly in bringing new projects to market, while still maintaining the appropriate systems and controls to manage risk. Regulators should be flexible enough in their approach to enable businesses to take advantage of innovation, but there will be a clear expectation that those businesses have considered all the relevant legal and regulatory issues and tested the robustness of their governance and risk management procedures.

Looking ahead

2016 saw the launch of a number of new business models that aim to revolutionise the distribution and underwriting of insurance. Some of the new start ups present a real challenge to the traditional broker model, as they look to simplify the distribution chain (although the 'death of the broker' is a familiar refrain). The role of insurers may also need to adapt as they are forced to work directly with technology companies and social networks that control new distribution platforms and therefore the interaction and relationship with the customer. Insurers with legacy IT systems which are not fit for purpose in dealing with the new technologies will be at a disadvantage and much delayed investment in new systems may be brought forward.

The impact of technology on product design and distribution is a priority theme for the FCA and EIOPA plans a series of insurtech roundtables in 2017 to help it understand the risks, benefits and obstacles to innovation. This will help the development of Europe's insurtech regulatory framework, which must balance support for innovation against maintaining standards of consumer protection and ensure that those who are not computer/ smart phone literate can still access suitable products.

For those participating in the UK insurtech sector, this may be seen as the ideal opportunity for the UK government and the regulators to demonstrate commitment to supporting the insurance sector. The swift approval of new market entrants or change of control approvals for acquisitions would be well received, together with an understanding of the flexibility required in the product governance models that are developed when testing new products. Creating a favourable regulatory environment could be one of the much discussed competitive advantages for the UK in the post Brexit world and should be considered together with fiscal and other initiatives designed to support the insurtech/fintech sector.

How we can help

Clifford Chance is a full-service global law-firm with market-leading insurance regulation, technology and insurtech/ fintech teams. Our in-depth knowledge of these business sectors means that we are ideally placed to advise clients on insurtech and the associated issues across M&A, joint ventures, commercial agreements, technology law, intellectual property, data protection, antitrust, finance and tax.

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