**AN INSURTECH GREENHOUSE: FUTURE US-UK REGULATORY AND FINTECH COLLABORATION**

**Paul Thanos Global Trade and Investment Fellow**

**Woodrow Wilson International Center for Scholars**

Insurtech will lead to more change in the insurance industry in the next ten to fifteen years than it has seen in the centuries since Edward Lloyd set up his coffee shop near the wharves in London in 1688 and began coordinating the writing of policies to cover ocean-going vessels.

Paul Carroll Editor and CEO Insurance Thought Leadership

As the Trump Administration begins to implement a new trade and investment agenda for the United States, all avenues should be explored in order to maximize opportunities for American businesses to expand, create jobs, and compete in international markets. 2016 has seen explosive growth in financial technology (fintech) companies both in the United States and around the world. Fintech refers to companies whose line of business combines software and technology to deliver financial services.[[1]](#footnote-1) Fintech companies include businesses focused on payments, blockchain, wealth management, crowdfunding, digital currencies, peer-to-peer lending, clearance and settlement, and most recently the insurance sector (insurtech). Automation, new sources of data, mobile technologies, and new insurance models are all changing how insurance companies do business.[[2]](#footnote-2) Many U.S. fintech companies consistently cite the lack of a clear and coherent regulatory structure within the United States as a major impediment to further growth and expansion. The power of fintech and insurtech to accelerate financial inclusion and provide greater financial security to the marginal and the unbanked is one of the greatest potential impacts of this segment of finance.

Fintech plays an essential role in expanding access to capital for citizens who may or may not have access to banks or more traditional financial services. Fintech can help address the growing program of “capital deserts” by providing citizens tools to access capital particularly in underserved rural and urban areas. Greater financial inclusion has been a key goal and objective of the G20 since at least 2009.

After reaching $19 billion in total in 2015, worldwide fintech funding hit $15 billion by mid-August 2016 with the United States, Europe, and the Asia-Pacific (APAC) region leading the way in attracting the most fintech investment. Accelerators and incubators set up by established financial services companies and their tech partners are encouraging this growth, as these programs place fintech companies on the cutting edge of business ideas, along with a first-mover advantage if they want to invest in or acquire startups. Fintech funding surged in 2016 due to tremendous funding rounds by Chinese fintechs along with expanded interest in insurtechs. Venture capital (VC) has traditionally dominated fintech funding but many of the largest funding rounds in 2016 were private, with corporate investors starting to increase their investments either in competition or coordination with VCs.[[3]](#footnote-3)

As the Information Technology and Innovation Foundation (ITIF) points out in its comprehensive article “Policy Principles for Fintech”, the financial services industry is an *information* industry where money is simply a nominal representation of real value (goods or services). Yet, compared with some information industries that reaped disruptive gains from information technology, the financial-services industry has experienced mostly incremental innovation. For example, the creation of the Internet enabled innovators to route voice traffic over Internet Protocol networks, changing telephony from an expensive, intermediary-driven system into the more efficient, globally interconnected system we have today. The financial services industry is potentially at a similar inflection point, where expensive, single-purpose networks and systems are giving way to cheaper, general-purpose ones.

The fintech businesses pushing this transformation promise improvements in financial-services industry productivity, greater ease and lower prices for consumers, and greater access for those now underserved by the financial-services sector. These innovations are poised to radically improve how consumers and businesses transfer money and make payments, store value, save and invest, borrow, and insure themselves against risk. But achieving this will require policymakers and regulators to actively support fintech transformation.[[4]](#footnote-4) A question for the Trump Administration will be how best to create an environment that will maximize the opportunities and innovative potential for American firms within this emerging segment of financial services. For the insurance sector specifically, the combination of Brexit with proposed changes in the federal role in both domestic and international insurance issues, create a once in a lifetime opportunity for the United States (both state regulators and the federal government) and the United Kingdom (UK) to create a 21st century approach to the intersection of insurance regulation and financial technology through the establishment of a cross-border insurtech greenhouse.

**Current fintech landscape – and growth of insurtech**

In 2015, the *Economist* estimated that there were over 4,000 active fintech start-ups around the world, and more than a dozen are valued at over $1 billion. McKinsey estimates that new entrants will increasingly battle for customers with incumbents over the next decade, with the top five banking businesses (i.e., consumer finance, mortgages, lending, retail payments, and wealth management) at risk of losing between 20 and 60 percent of their profits by 2025.[[5]](#footnote-5) Existing financial institutions are also embracing fintech, with some financial institutions choosing to form strategic partnerships with technology companies.[[6]](#footnote-6)

As noted above, one of the most noteworthy trends within fintech has been the emergence of insurtech. Developments in technology are leading to new methods in service provision as well as greater opportunities for data collection and better risk and mitigation measures. Insurance claims can be processed through online platforms, and comparative sites permit product comparison of various insurance products.[[7]](#footnote-7) The growth of insurtech businesses has been fueled by new digital capabilities and Internet of Things (IoT) devices that are reducing costs, changing systems and processes and enhancing the consumer experience. Examples of connected devices include telematics devices in cars that transmit data about driving habits, connected water detection and security systems in the home, and wearable health-monitoring units such as home blood pressure monitors. As the cost of sensors falls and global internet connectivity increases, the number of connected devices is likely to grow substantially over the next five years – all of which will could provide insurers with both direct access to and real-time data about policyholders, potentially disrupting insurance distribution channels. [[8]](#footnote-8)

Steeped in tradition and burdened by outdated systems and paper-based operations, the insurtech space has emerged as one of the largest innovation ecosystems globally in 2016, with $4.74bn (470 deals) invested in the space since 2011, according to [CB Insights](https://www.cbinsights.com/reports/ITC-insurance-tech-deck.pdf).[[9]](#footnote-9) The key is insurtech provides the industry – including both established insurers and new insurtech start-ups - a means of accommodating the modern consumer. As Thomas McCourtie, financial analyst at Global Data has explained “The industry is looking to fall in line with other areas of commerce by providing consumers with quicker and more efficient services. Insurtech acts as the facilitator in developing new propositions which enable customers to obtain cover without the need to contact an advisor, and can be arranged remotely on a mobile device. Good examples of this include the many online or app-based peer-to-peer platforms emerging from this space, which encourage users to group together and collectively share risk, often without the services of an underwriter.”[[10]](#footnote-10) Insurtech companies vary widely from those providing new digital ecosystems to expedite compliance and verification processes, to brokerage companies offering P2P platforms for consumers to obtain insurance, to licensed providers using mobile technology to provide insurance services in developing markets. But major challenges persist that are preventing even more explosive growth of insurtech, including high barriers to entry, gaps in regulatory supervision in other markets, and complicated regulatory structures in the United States and other parts of the world. For example, regulatory frameworks were often designed for older business models and are slow to adopt change. Firms operating internationally frequently contend with restrictions on where they can store and transmit data and with regulations designed to protect domestic incumbents. In the United States, where insurance is regulated at the state level, requirements can differ state to state making the nationwide development and marketing of a new insurance product a tedious and expensive process. The broader financial-services sector also continues to face a number of evolving security threats, from data breaches to large-scale theft and fraud.[[11]](#footnote-11) Fortunately, an opportunity exists in the United States for both business and government at the federal and state level to innovate in a new and productive way.

**U.S. INSURTECH COMPANIES AT A GLANCE**

**GaPro**

* First industry-wide disruptive digital ecosystem designed for the compliance and verification process.
* Based in Southfield, Michigan GAPro’s platform improves speed of data sharing, automating compliance checking and efficiency.
* GAPro normalizes insurance data, simplifying digital connection and enabling automated compliance checking. Self-service verification of insurance tells everyone that coverage is in place and meets their needs starting when they need it and moving forward -- not as of a point in time as indicated on a paper certificate.
* Detecting potential non-compliance, GAPro notifies stakeholders, enabling exception processing instead of manual review of all certificates.
* The change will take out a whole layer of cost while making the data far more valuable and enable a world where you just look at an app and get an up-to-the moment result.
* http://gaprosystem.com/

Source: Insurance Thought Leadership

**Risk Genius**

* Overland Park, Kansas based company uses artificial intelligence to analyze policies clause by clause, as opposed to just word by word.
* Makes brokers more efficient by helping them compare coverages from different carriers and by largely automating the analysis.
* Will allow for much faster innovation in policies greatly reducing time and allowing for faster innovation.
* RiskGenius' high-level analysis at the clause level will also give consumers a way to better understand their policies, rather than drowning them in legalese.
* https://riskgenius.com/

Source: Insurance Thought Leadership

**International Agreements and domestic legislation**

The Dodd-Frank Financial Reform Act of 2010 authorized the Treasury Secretary and the United States Trade Representative (USTR) to jointly conclude a written bilateral or multilateral agreement with foreign governments, authorities, or regulatory entities on "prudential measures with respect to the business of insurance or reinsurance[[12]](#footnote-12)". Under that authority in January 2017 the Treasury Department and the US Trade Representative (USTR) concluded its first insurance “covered agreement” with the EU that purports to resolve the disparate treatment of U.S. insurers operating in EU member states and eliminates collateral requirements for EU insurers in the United States. Under this agreement, the material differences from current state credit for reinsurance laws could potentially lead to a preemption of state laws. The covered agreement covers three areas of "prudential insurance" oversight: (i) reinsurance (insurance purchased by an insurance company); (ii) group supervision (supervision of holding companies with insurance units); and (iii) the exchange of insurance information between supervisors. The US-EU Covered Agreement comes at a time where members of Congress have proposed legislation that would have a dramatic impact on both insurance and fintech. For example, Congressman Jeb Hensarling has introduced the Financial Choice Act which would consolidate how insurance is addressed at the federal level by creating an Independent Insurance Advocate (IIA) within the Treasury Department. The IIA would serve as the voting Financial Stability Oversight Council (FSOC)[[13]](#footnote-13) member and would coordinate federal efforts on the prudential aspects of international insurance matters, including representing the United States at the International Association of Insurance Supervisors (IAIS) and assisting in the negotiations of covered agreements. The IIA would also consult with state insurance regulators regarding insurance matters of national importance and prudential insurance matters of international importance.

And while not directly related to insurance other legislative and regulatory initiatives related to fintech include legislation sponsored by Congressman Patrick Kennedy (R-NC) that would require many federal agencies including the Federal Reserve Board, the Treasury Department and the Securities and Exchange Commission to develop an internal “Financial Services Innovation Office” where companies can seek help in testing a product. In December 2016 the Office of the Comptroller of the Currency (OCC) published and solicited comments for a paper exploring special purpose bank charters for fintech companies.

At the state level the National Association of Insurance Commissioners (NAIC) announced in early March 2017, the creation of the Innovation and Technology (EX) Task Force. The Task Force will provide a forum for the discussion of innovation and technology developments in the insurance sector, including the collection and use of data by insurers and state insurance regulators—as well as new products, services and distribution platforms—in order to educate state insurance regulators on how these developments impact consumer protection, insurer and producer oversight, marketplace dynamics, and the state-based insurance regulatory framework.

**An Insurtech greenhouse**

The tremendous potential of fintech should cause regulators to find the right balance between fostering innovation and protecting consumers. As the OECD has pointed out in its report on technology and innovation in the insurance sector, there are regulatory and competition considerations that need to be made as disruption to the industry is often about new market entries as well as new modes of service provision which may not fit the mode in which regulations were originally conceived. There are also wider privacy and data protection issues which require close attention given that insurtech usually involves a digital component to the technology. [[14]](#footnote-14)

The US-EU covered agreement is historic in many respects, but Brexit would remove the UK from obligations negotiated within the Covered Agreement and require both countries to seek a new agreement to discuss bilateral prudential related insurance issues. The UK has already established a fintech “regulatory sandbox” to provide a mechanism for fintech firms (including insurtech companies) to test products, services, business models and delivery mechanisms without fear of enforcement actions or regulatory reprisals whose impact can be devastating to a start-up firm with limited capital.

On January 26, 2017 UK’s Financial Conduct Authority (FCA) Chief Executive Andrew Bailey gave remarks at the Economic Council Financial Markets Policy Conference in Berlin where he stressed the need for global regulatory standards as the basis to govern market access for financial services firms. And in February 2017, the UK FCA and the Ontario Securities Commission of Canada signed an agreement to share information on regulatory issues and trends impact fintech. This agreement between Canada and UK provides a template for the first true cross-border regulatory collaboration within the fintech space. Currently the United States does not have a similar cross-border mechanism in place.

Given that the Trump Administration is evaluating international agreements, and an opportunity will soon present itself to partner with a country with experience in establishing a regulatory sandbox, serious consideration should be given to the creation of an US-UK insurtech cross border regulatory “greenhouse.” (a greenhouse connotes an environment where living things can grow and be nurtured as opposed to a sandbox which delineates boundaries). Initially established as a pilot project, the Greenhouse would provide an opportunity for both U.S. and UK insurtech companies to beta test products, provide regulators with data resulting from those tests and ensure that the data is protected, and then determine jointly which companies are prepared for chartering and licensing.

The vehicle to establish the Insurtech greenhouse could be part of a new bilateral pro-FinTech Co-operation Framework between the state insurance regulators in the United States and the UK FCA. The Department of Commerce could play an important role in promoting and highlighting ways that new insurtech companies would gain access to the greenhouse. In addition, consideration could be given to the inclusion of Global insurance accelerators such as those that exist in Des Moines, Iowa or New York City in a consultative capacity. These Accelerators – supported by insurance providers and brokers - are already playing an important role in preparing start-ups to compete in global insurance markets. Finally, if a new pro-FinTech Co-operation Framework  is not the right vehicle to establish the Greenhouse – a regulatory cooperation chapter within a new US-UK Free Trade Agreement could be a another opportunity to give FTAs a fresh look and modernize commitments and structures to support new industries. Successful creation and execution of the Insurtech Greenhouse could result in the United States pursuing similar collaborations with other countries who have established innovative approaches to fintech regulation including Singapore, Hong Kong, Canada, Israel and the United Arab Emirates.

**Future is now**

President Trump has signed an executive order requesting that the Secretary of the Treasury review regulations on financial institutions and to report back to him on specific recommendations to the President. Many of these regulations were those inaugurated by the Dodd Frank Financial Reform Act of 2010. Both the executive branch and Congressional reviews of the regulatory structure of the financial services industry, combined with the rapid growth of financial technology, and the opportunity for new exclusive collaboration with the UK following Brexit, create an ideal environment for new approaches in order to better position regulatory assets to both support innovation and protect the consumer.

According to Alex Ross, author of “Industries of the Future” there are currently 20 billion networked devices around the world – and in three years that number will more than double and total 45 billion. The growth of fintech is directly correlated to the expansion of networked devices – and show no sign of slowing down. What does slow down fintech – and with it U.S. economic competitiveness – is a regulatory framework that is slow to adapt to new technologies and to adjust to how the power of modern communications has forever changed business models. Insurance regulation is complex and international insurance dialogue will mandate cooperation now only between different countries but also between federal and state authorities. The burden should be on government and regulators to make the effort, and in the end create an environment that can support these new business ventures in a safe and secure way while expanding access to the uninsured and the underinsured. At least as a pilot project, we should engage with the UK to learn, share best practices, and empower insurtech greenhouses to “let the flowers bloom.”

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