SLAUGHTER AND MAY/

CLIENT BRIEFING

JANUARY 2024

INSURANCE OUTLOOK 2024

In this briefing we look ahead to some of the key themes likely to affect the insurance sector in 2024.

2024 - An election year

In looking ahead at the outlook for 2024, it is worth bearing in mind that a general election will take place this year. The prime minister has recently suggested that an autumn election is the most likely timing for this.

Based on current polling, a Labour-led Government is predicted to come into power for the first time since 2010. The immediate impact that this would have on the legislative and reform agenda for the insurance sector during 2024, as set out by the Conservative-led Government to date, will partly depend on the timing of the election. It seems reasonable to assume, however, that even if a Labour Government comes into power, in the short term it would continue to support many reforms and measures relevant to the insurance sector that are already being implemented or consulted upon, in the interests of stability.

Elections are also due to take place in the European Parliament – these are set for 6 to 9 June 2024, and will trigger the formation of a new European Commission and new leadership in the Council. Prior to the elections (up until the end of April at the very latest) the EU institutions will focus on finalising Level 1 legislative files which are currently in trialogue as much as possible, and after the elections on defining a new work programme for the term of 2024 to 2029. Past experience suggests that the new Commission and Parliament will resume work at the earliest after the summer break in September and potentially as late as December.

Progress on some of the insurance related Level 1 legislation has been slow during 2023 but on 13 December the Council of the EU and the European Parliament announced provisional political agreement on proposed amendments to the Solvency II Directive and on the new Insurer Resolution Directive. The next step will be for the agreement on the texts to be confirmed by the Committee of Permanent Representatives and by the Parliament. These legislative files may therefore be finalised prior to the Parliamentary elections. It seems likely that there will be a delay, however, in publication of European Commission proposals for amendments to the Solvency II Level 2 Delegated Regulation, which is the next step in reforms to the Solvency II regime.

Pension derisking developments

Levels of activity in the UK pensions derisking market in 2023 have eclipsed previous records, both in terms of overall volumes (which are expected to significantly exceed the previous record of £43.9bn in 2019) and deal size. These trends are expected to continue. Projections are that deal volumes could exceed £60bn in 2024, supported by the dramatic improvement in scheme funding levels in a higher interest rate environment and the continued appetite of insurers to write more and larger deals.

The work we were involved in during 2023 reflected these trends: RSA/Intact's £6.5bn full buy-in of two schemes was the largest bulk annuity transaction from pension schemes to an insurer to date; Tata Steel UK's de-risking of the British Steel Pension Scheme covered c. £7.2bn of liabilities in aggregate and was the largest fully bought in pension scheme to date; and Legal and General's £4.8bn buy-in of the Boots Pension Scheme was the largest single transaction of its kind by premium size to date.

We have also been involved in significant reinsurance transactions in respect of pension deriskings, which is an area of ongoing regulatory focus for the PRA, as reflected in its recent consultation (CP24/23 – Funded reinsurance) - discussed in our November briefing.

The landscape of the market is evolving, with the potential for additional capacity from further new entrants (following M&G's re-entry after a seven-year absence), insurers becoming more selective in how they deploy their resources prior to entering exclusive negotiations, and greater levels of regulatory intervention. Over the coming year, alongside supporting our clients through high levels of transactional activity, we will be monitoring the increased scrutiny being applied by the PRA to life insurers in this market, including the outcome of CP24/23.

We expect that the level of growth in this market will continue to attract interest from potential investors, both in respect of those providers with established positions and others (such as private equity) with a broader interest in participating in the market. In addition, there is the potential for political events this year to impact the market environment, as well as scope for the policy on interest rates to affect the levels of scheme funding.

M&A

We are cautiously optimistic that 2024 will see an increase in M&A activity, relative to the decreased levels experienced in 2023 against a backdrop of market volatility, high inflation and rising interest rates. This includes ongoing strategic acquisitions and disposals, as companies look to dispose of non-core businesses and consolidate their core businesses and markets, or seek bolt-on acquisitions to support ESG, insurtech and digital transformations. Though high interest rates are expected to remain for some time, a stabilisation of interest rates may lead private equity sponsors to take advantage of market conditions to deploy unprecedented levels of dry powder accumulated due to the slow-down of activity in 2023, notwithstanding the increased cost of debt finance. We may also see private equity exits in 2024, as sponsors look to crystallise their investments.

Solvency UK

Solvency UK will be introduced in stages over the course of 2024. The amendments to the risk margin methodology came into effect on **31 December 2023**, potentially allowing a significant release of capital by firms. The impact on balance sheets in the short term will depend on a number of factors, including the current application of transitional measures on technical provisions. Changes to the matching adjustment are expected to come into effect at the **end of June 2024**. It is hoped that the combination of these changes will allow insurers to invest large amounts of capital into productive assets such as infrastructure – an ambition supported by industry groups such as the Investment Delivery Forum.

The remainder of the Rulebook changes will be implemented from the **end of 2024**. Some of these are yet to be consulted on – the PRA plans to publish a further consultation in Q1 2024, although this is not expected to contain substantive changes to the rules. Practitioners will nevertheless be interested in the detail of how relevant European legislation and guidance will be transposed into the UK regime.

Captive insurers – a new framework?

In his Autumn Statement, the Chancellor included an announcement that the Government will consult in Spring 2024 on the design of a new framework for encouraging the establishment and growth of captive insurance companies in the UK.

The introduction of a new regime for captive insurers has been lobbied for by the London Market Group (which is supported by the International Underwriting Association of London, Lloyd's of London, the Lloyd's Market Association and the London & International Insurance Brokers' Association) and was included as a priority in its 2023 Plan for the Future. In that document the LMG states that there are currently no captive insurers in the UK and argues that this is the result of a regulatory system which does not differentiate between captives and other insurers. In principle, captives present a lower risk to the overall financial system because they only write risks belonging to their own corporate group.

No details of any potential future framework have been released by the Government at this stage but the expectation would be that captives would have more streamlined governance and reporting, and possibly lower capital, requirements. This would encourage UK based corporates and public sector bodies to use onshore captives, among other things reducing the transfer of assets overseas. The creation of a 15% global minimum tax rate has reduced the incentive to locate captive insurers overseas, albeit the UK tax rate on captive insurance profits (25%) remains rather higher than the tax rate in, for example, Bermuda. While unlikely in the current political climate, a reduction in the UK rate for captive insurers (as the UK has already done for patent income) would provide further support for this initiative.

In parallel with this, Lloyd's has been promoting its market-place for the establishment of captive syndicates. It is understood that none are currently in place, but existing structures within Lloyd's would allow captive syndicates to use Lloyd's international underwriting permissions and, where relevant, to share the financial strength rating of the Lloyd's market. Capital would be provided to the captive syndicate by its corporate group, via a UK corporate member at Lloyd's.

The Consumer Duty and closed books

> "a reasonable interpretation of fairness should include a more holistic consideration of the overall outcome being delivered today rather than rely solely on something that was promised many years ago and which is embedded into a contract's T&Cs"
>
> *The FCA, FG 16/8 Fair treatment of long-standing customers in the life insurance sector (December 2016)*

Legacy products, or closed-book business, has been an ongoing regulatory focus for the FCA for a number of years. The FCA first announced a thematic review of closed books in its 2014/15 Business Plan, culminating in the publication of FG 16/8. That guidance focuses on aspects of the customer journey such as clear and timely communications, switching of products and consideration of fund performance.

The implementation of the Consumer Duty for closed books is likely to require additional action by firms. Whilst the FCA has said repeatedly that the duty will not infringe vested rights and that firms will not be judged with the benefit of hindsight, firms do need to consider the price and value outcome in respect of their closed products. This includes considering whether "there is and remains a reasonable relationship between the price customers pay and the benefits of the product or service". The FCA's guidance (in FG 22/5) on what constitutes a vested right suggests a relatively limited scope – it comments, for example, that "where a customer can terminate a contract without an exit charge, firms have no more than an expectation of the customer continuing the contract"; future contractual rights are therefore not necessarily vested.

Potential solutions proposed by the FCA where issues are identified but vested rights apply include providing greater flexibility on how customers can engage with a product or assisting a customer to switch to a new product or service that does not have the same issues. The guidance does not give clarity on how firms should address vested rights where these options do not address the issue identified, or on situations where a firm has contractual but not vested rights and the assessment of the product fails the price and value outcome test. In the 2016 guidance, the FCA stated that firms were not being required to amend their T&Cs in light of current regulatory requirements, or to dis-apply or amend T&Cs to reflect the changing expectations of customers. It does appear that the ground has shifted somewhat, and firms with closed books may have work to do between now and the end of July to ensure they meet the required standards.

Key dates

12 January 2024	Deadline for responding to PRA CP21/23 – Approach to authorisation and supervision of insurance branches
16 February 2024	Deadline for responding to PRA CP24/23 – Funded reinsurance
Q1 2024	Expected publication of HM Treasury draft statutory instrument enabling the FCA to deliver the new retail disclosure regime (replacing PRIIPs)
Q1 2024	Expected publication of the PRA's final consultation on implementation of Solvency UK

Spring 2024	Expected Government consultation on a new framework for encouraging the establishment and growth of captive insurance companies
31 May 2024	FCA anti-greenwashing rule comes into force
30 June 2024	Statutory instrument implementing matching adjustment changes comes into effect and accompanying PRA Rulebook changes expected to come into effect
31 July 2024	Extension of the Consumer Duty to closed products and services
H1 2024	Expected PRA consultation on exit planning for insurers
2024	FCA consultation on the new retail disclosure regime replacing PRIIPs
2024	FCA post-implementation review of its guidance on the fair treatment of vulnerable customers
2024	Possible legislation implementing a new insurer resolution regime
31 December 2024	Expected implementation of the full version of Solvency UK, including all amendments to the PRA Rulebook and revocation of relevant onshored EU legislation

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