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Briefing note

Key regulatory updates: Life and General Insurance late 2016/early 2017

Many New Year's resolutions are no doubt long forgotten by now, but the regulatory publications from the last quarter of 2016 and the first couple of months of 2017 may be with us a little longer.

In case you missed anything amid the rush to prepare for and get stuck into year-end reporting, this newsletter highlights the main points from some of the key regulatory publications between the period 1 October 2016 to 28 February 2016.

Each section heading indicates whether the publication is applicable to:

Life insurers General insurers Both

1. PRA activity

1.1 Solvency II: Reporting format of National Specific Templates and reporting clarifications

In November 2016, the Prudential Regulation Authority (PRA) released consultation paper CP40/16 followed swiftly in December by policy statement PS38/16 setting out final rules on National Specific Templates (NSTs). The policy statement contains the following rules regarding year end reporting:

- For financial year-end 2016 and subsequent submissions, firms are required to submit their NST information in an 'XBRL-enabled' Excel workbook that is available on the PRA website, along with log files containing guidance on how to complete them
- The style of the NRTs has been updated to better mirror that of the Quantitative Reporting Templates (QRTs) required by the European Insurance and Occupational Pensions Authority (EIOPA)

It should be noted that an earlier consultation by the PRA (CP37/16) suggested that firms should report NSTs in full XBRL format by financial year-end 2017 and could adopt full XBRL earlier if desired. The PRA took the unusual action of withdrawing CP37/16 and a full XBRL submission is not currently allowed. The PRA's intention is still to move to full XBRL reporting in the future, and it will consult on this at a later point in time.

1.2 Solvency II: Consolidation of Directors' letters

Between 1 April 2013 and 15 February 2016, the PRA drip-fed its expectations of firms preparing for various aspects of Solvency II in line with emerging best practice. Following a consultation earlier in 2016, (CP20/16), all relevant guidance and expectations from the directors' letters were consolidated into an array of supervisory statements published alongside Policy Statement PS33/16 as follows:

- **SS17/16 – Solvency II: Internal models – assessment, model change and the role of non-executive directors**

  The supervisory statement proposed in CP20/16 had sections outlining the PRA's quantitative framework for assessing internal models for approval as well as technical details of specific quantitative indicators it uses. Following feedback, the PRA recognised that its quantitative indicators, and therefore anything written about them, will change over time and consequently has excluded the technical details from the final version.

  SS17/16 has also been updated from the proposals to alert readers that details of model changes are covered in a separate supervisory statement (SS12/16 – Solvency II: Changes to internal models used by UK insurance firms).

- **SS18/16 – Solvency II: Longevity risk transfers**
  No changes have been made to the draft supervisory statement proposed in CP20/16. In PS33/16 the PRA clarified that not all firms are expected to follow a single approach to longevity risk transfer, however firms must assess the risk and capital implications of their chosen approach. The PRA will consider whether a particular longevity risk transfer renders the standard formula invalid for individual firms on a case-by-case basis.
- **SS19/16 – Solvency II: ORSA**
  In PS33/16 the PRA reiterated that the ORSA is primarily a process for firms to understand and manage their business, risks and capital appropriately and consider that this is reflected in SS19/16. PS33/16 also clarified that firms should consider their own risks and capital from their own perspective, as well as on a regulatory basis. The ORSA report should evidence firms' ORSA processes and should include an accurate record of decisions taken by the board at any given time.
- **SS20/16 – Solvency II: Reinsurance – counterparty credit risk**
  The PRA amended SS20/16 to clarify that while all firms are expected to manage and, as necessary, mitigate the effects of concentration of credit risk concerning reinsurance cover, the considerations may differ between large and smaller firms.

  The PRA reiterated in PS33/16 that the standard formula does not always sufficiently reflect the risks within some reinsurance arrangements, and firms should consider whether this is material when assessing standard formula appropriateness. In PS33/16, the PRA also categorically denied seeking to introduce termination or recapture clauses linked to the SCR as a means of managing counterparty concentration risk. These comments are not reflected in to SS20/16.
- PS33/16 made no material changes to the updates proposed in CP20/16 for the following supervisory statements:
  - SS2/14 – Solvency II: Recognition of deferred tax
  - SS7/15 – Solvency II: Transitional measures on risk-free interest rates and technical provisions
  - SS2/14 – Solvency II: The treatment of pension scheme risk

1.3 Solvency II: Monitoring drift and standard formula SCR reporting for firms with an approved internal model tool

The PRA has published supervisory statement SS15/16 on monitoring drift and standard formula SCR reporting for firms with an approved internal model. The PRA has made the following material changes and clarifications to the proposals in its original consultation on the subject.

- The PRA monitors internal model drift using an array of metrics, including model drift ratios. The original proposals suggested that these ratios would be re-based after each change in risk profile and each major internal model change. The PRA has now clarified that these events will only trigger a re-base in the ratios if they result in a material change in the firm's SCR
- The PRA originally proposed that firms using an internal model to calculate their solo SCR also needed to report their solo SCR as calculated using the standard formula. The PRA has clarified that the standard formula calculation of the SCR will be private between the firm and the regulator. This standard formula calculation does not need to be externally audited, however it does need to be approved by senior management
- The PRA originally proposed that the additional standard formula SCR calculation results should be submitted at the same time as the firm's annual quantitative reporting deadline. The PRA has changed this to give firms an additional four weeks

1.4 Changes to PRA rulebook

In October 2016 the PRA released occasional consultation paper CP36/16, which sets out proposed changes to the PRA rulebook. Of most relevance to insurers are changes to rules concerning capital issuance (chapter 3 of the consultation paper) and external audit (chapter 7).

Chapter 3 consulted on the PRA's proposals to make clarifications and corrections to the PRA Pre-Issuance Notification (PIN) rules within sections of the PRA Rulebook. For capital issuances that make use of the debt securities programme drawdown exemption or previous issuance exemptions, the proposed rules clarify that Solvency II firms are required to provide, as soon as practicable after issuance of the instrument:

- final terms and conditions;
- final opinions;
- a reasoned basis for coupon structure; and
- any other provision that might suggest an incentive to redeem.

The PRA also proposed to amend the PIN rules to clarify that if the terms and conditions have not changed since a previous issuance, no confirmation from the firm is required.

Chapter 7 proposed minor corrections to the External Audit Part of the PRA Rulebook. The PRA proposed to add a definition for 'group supervisor' to External Audit 1.1. This definition was not included in the PRA's September 2016 policy statement PS24/16 on external audit for Solvency II firms. The PRA also proposed to amend External Audit 4.1(3) so that the rule fully conforms to the International Standards on Auditing ('ISA'), following previous changes to the rules and supervisory statement made in PS24/16 to conform to ISA.

This consultation closed on 11 January 2017.

1.5 Reporting instructions for non-Solvency II firms (except friendly societies)

The PRA released supervisory statement SS14/16 in October 2016 setting out the reporting requirements for firms that are outside of the scope of Solvency II and are not friendly societies. This follows the PRA's consultation paper CP18/16, published in May last year, which consulted on revisions to the required submissions (which are broadly equivalent to the old 'PRA Returns' but with some amendments including removal of the more granular information). Although no feedback was received from the consultation paper, the regulator made a few amendments to the draft supervisory statement:

- SS14/16 now includes references to the sections of the PRA rulebook which should be read in conjunction with the supervisory statements
- Additional clarification is given on the PRA's expectation of firms regarding the use of supplementary notes. Firms are expected to submit supplementary notes to a form as a separate statement. Supplementary notes should include all applicable codes and be provided to the PRA in accordance with the requirements set out in the supervisory statement's appendices
- The style and structure of the supervisory statement has been changed to align with other similar PRA reporting instructions

The majority of the information within the statement steps through the requirements to complete each of the required submission forms. These are clearly identified within the appendices.

1.6 Solvency II: Group supervision

The PRA issued CP38/16 on 7 November 2016. This consultation proposes updating Supervisory Statement SS9/15 ('Solvency II: Group supervision') to reflect material previously set out in the PRA's letter 'Solvency II: An update on implementation'. The consultation also proposes to update SS9/15 with references to the PRA rulebook and to take account of certain aspects of the Solvency II regulations.

Firms are already required to provide an analysis of the availability of own funds to absorb losses within the group in their Solvency and Financial Condition Reports (SFCRs) and Regulatory Supervisory Reports (RSRs). The PRA expects this analysis to be available to support the solvency position reported at each reporting date.

The PRA expects groups to provide robust and credible evidence that the apparent availability of own funds at the group level is not compromised or effectively undermined by any legal or regulatory restrictions on transferability. Furthermore, firms are expected to provide evidence that own funds can be transferred and made available to the group within a maximum of nine months.

If a group intends to utilise own funds from a third-country related undertaking, then the PRA expects both local and Solvency II rules to be taken into account.

This consultation closed on 7 February 2017.

1.7 Solvency II: Maintenance of the transitional measure on technical provisions

On 15 December 2016, the PRA released CP47/16 with proposals to amend SS6/16 regarding the maintenance of the transitional measure on technical provisions (TMTP) under Solvency II. Firms continue to have to apply for approval to use the TMTP. The PRA's proposed changes can be grouped under the following headings:

- Analysing the TMTP
- Consistency of Solvency I and Solvency II bases
- Recalculation of the transitional measure

This consultation closed on 15 March 2017

1.8 Solvency II: Matching adjustment – illiquid unrated assets and equity release mortgages

In consultation paper CP48/16 the PRA reminds firms that any internal credit assessment processes used for assets in matching adjustment (MA) portfolios should be independently reviewed. Internal ratings are required for assets which do not have a rating from an External Credit Assessment Institution (ECAI). These internal ratings should be broadly consistent with the ratings that ECAIs would produce i.e. they should lie within the plausible range of a rating given by an ECAI. Fundamental spread mapping should reflect both quantitative and qualitative risks posed, which may require adjustment to internal ratings.

The PRA's monitoring of internal ratings will focus on:

- Complex rating processes e.g. where assets have been restructured
- Assets where the absolute value of the MA benefit is material to the firm
- Assets where the MA benefit is a high proportion of the total spread, either in its own right or relative to comparable assets

There will also be a focus on the internal credit assessment of equity release mortgages (ERMs).

CP48/16 also sets out the PRA's expectations regarding the risks from embedded guarantees in ERMs based on the following principles:

- Securitisations where firms hold all tranches do not result in a reduction of risk to the firm
- The economic value of ERM cash flows cannot be greater than either the value of an equivalent loan without a no negative equity guarantee (NNEG) or the value of future possession of the property providing collateral
- The value of future possession of a property should be less than the value of immediate possession
- The compensation for the risks retained by a firm as a result of the NNEG must comprise more than the best estimate cost of the NNEG

This consultation closed on 14 March 2017.

1.9 Cyber risk

The PRA consulted on proposals to introduce a new Supervisory Statement setting out its expectations for the prudent management of cyber underwriting risk. This was accompanied by a letter to firms highlighting the results of the thematic review underlying the proposal. The proposal covers three broad areas:

- **'Silent' cyber risk** - This is the implicit cyber exposure within 'all-risks' and other liability insurance policies that do not explicitly exclude cyber risk. The PRA's thematic review concluded that:
  - there is an almost universal acknowledgement by firms of the potential loss due to 'silent' cyber risk;
  - the potential for a significant 'silent' cyber risk insurance loss is increasing over time;
  - casualty (direct and facultative) and marine, aviation and transport lines of business are potentially significantly exposed to such losses; and
  - the exposure and response of reinsurance contracts to 'silent' cyber risk is uncertain.

  The PRA proposes that firms must have the ability to monitor, manage and mitigate 'silent' cyber risk effectively.
- **Cyber risk strategy and risk appetite** - Firms exposed to 'silent' and affirmative cyber risk will need to have clearly articulated strategies and risk appetites on the management of the associated risks
- **Cyber expertise** - Firms need to have sufficient expertise to monitor and manage the risks emanating from cyber risk

The consultation closed on 14 February 2017.

1.10 Lloyd's managing agents

Following its consultation in July 2016, the PRA has now issued policy statement PS35/16. Although mainly focused on the banking sector, the statement includes changes to the conditions governing business rules for Lloyd's managing agents.

PS35/16 deletes the PRA's Conditions Governing Business (CGB) rule 12.5, which requires the Actuarial Function of each managing agent to review and provide an opinion on the adequacy of the technical provisions held by each syndicate managed by the managing agent in respect of general insurance business for each syndicate year (other than a closed year). This is because the actuarial function is already required to carry out detailed work on the Solvency II technical provisions and write an annual report to the governing body under the Solvency II rules.

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It should be noted that although the deletion of CGB 12.5 removed the provision of an opinion on the adequacy of the technical provisions as a PRA requirement, the Lloyd's valuation of liabilities rules as at year-end 2016 made it clear that the signing actuary opinion continues to be necessary as a Lloyd's requirement.

PS35/16 also amends one of the notification requirements to ensure that each managing agent informs both the Society of Lloyds and the PRA promptly of any concerns about the adequacy of the technical provisions, or of any material deficiencies, that are identified in the annual written report submitted to their governing body.

1.11 Solvency II: Regulatory reporting, internal model outputs

The PRA released an updated supervisory statement SS25/15 in February 2017 following its 2016 consultation paper CP31/16. The update provides further clarity on the information to be reported to the PRA on templates IM.01 and IM.03 by firms using an internal model.

1.12 Solvency II: ORSA and the ultimate time horizon – non-life firms

Also updated following CP31/16 was supervisory statement SS26/15 on ORSA and the ultimate time horizon for non-life firms. The updated supervisory statement gives firms the option to demonstrate that they have considered the ultimate time horizon in their ORSA supervisory report using PRA templates IM.03, MO.02 and MO.03.

2. FCA activity

2.1 Reviewing the funding of the FSCS

In mid-December 2016, the FCA issued consultation paper CP16/42 regarding a review of the funding and coverage of the Financial Services Compensation Scheme ('FSCS').

The consultation explores possible changes to the scheme including aspects that some might find radical such as the introduction of risk-based levies and that product providers might help fund claims caused by intermediary defaults.

The consultation is open until the end of March 2017 with a policy statement and further consultation expected in the autumn.

2.2 Removing ineffective disclosure requirements in the FCA handbook

The FCA has released policy statement PS16/23 removing disclosure requirements which it deems to be ineffective. This follows a discussion paper published in June 2015.

As of 22 November 2016, with-profits firms are no longer required to produce a Consumer Friendly Principles and Practices of Financial Management. They may continue to do so if they wish, but there is no regulatory obligation.

As of 27 March 2017, the Initial Disclosure Document, Combined Initial Disclosure Document and Services and Costs Disclosure Document templates will be removed from the FCA handbook. However, the policy statement notes that the Insurance Distribution Directive will introduce new disclosure requirements including the Insurance Product Information Document for non-life products.

2.3 Feedback on smarter consumer communications

The FCA's feedback statement on smarter consumer communications provides a general view of its expectations regarding firms' communications with customers. The paper focuses on ensuring effective communication and highlights the varied approach to and preferences for receiving information. The FCA now sees digital communication as an essential way to provide information to the newer generations of financial clients, and the need for effective disclosure will continue to be an area of scrutiny in 2017.

2.4 The FCA's future mission

The FCA has consulted on its future mission, which will set out the framework in which it will meet its Parliamentary objectives. The consultation will be used to establish a set of guiding principles that explain how the FCA pursues its statutory objectives; how it decides on its priorities and the tools it will use to meet its targets.

The consultation paper is looking for stakeholders' views on:

- how the FCA can ensure markets function well;
- whether the FCA's intervention framework is appropriate;
- how it can strike the right balance between its regulatory responsibility and broader public policy;
- whether its approach to consumer protection, vulnerable consumers and consumer redress is the right one;
- the role of consumer disclosures and whether a more 'interventionist' approach may be necessary on occasions;
- when the FCA should intervene;
- how the FCA supervises firms and enforces its regulations;
- the need for a more specific FCA handbook review, in light of the discussion around the issues above.

The consultation closed on 26 January 2017.

2.5 Transaction cost disclosure in workplace pensions

In October 2016 the FCA published CP16/30 on transaction cost disclosure in workplace pensions. The consultation paper proposed rules and guidance to improve the disclosure of transaction costs in workplace pensions.

The proposed rules set out a standard way in which to disclose transaction costs. On request by an operator of a relevant scheme, trustees/managers of an occupational pension scheme or another firm seeking to comply with its obligations, firms will be required to:

- Calculate the transaction costs incurred in the arrangement or investment vehicle to which the request relates. Transaction costs are defined as "the difference between the price at which an asset is valued immediately before an order is placed into the market (arrival price) and the price at which it is actually traded (execution price)"
- Provide both an aggregation of the transaction costs and a breakdown of the identifiable elements of the costs. The breakdown should at least include taxes, explicit fees and charges, and costs in connection with securities lending and borrowing
- Disclose administration charges

- Provide other relevant information. There are no specific information requirements here, but firms should use discretion based on the composition of each particular arrangement
- Respond in a reasonable timeframe and in an acceptable format

If the firm does not have the information necessary to comply with the above then it must take reasonable steps to obtain that information. If it is still unable to obtain it, the firm must provide a written explanation to the requesting party explaining why, including the percentage of investments in the arrangement for which information cannot be obtained, and indicating the categories of investment involved.

The consultation closed on 4 January 2017, and a policy statement is expected in the second quarter of 2017.

2.6 Finalised guidance on fair treatment of closed-book customers

On 9 December 2016 the FCA published FG16/8, which contains finalised guidance on fair treatment of long-standing customers in the life insurance sector. The guidance sets out the actions which the FCA believes life insurers must take to ensure that holders of life insurance products that are closed to new business are treated fairly.

The guidance focuses on four high-level outcomes:

- **Strategy and governance framework** – This must take proper account of the fair treatment of closed book customers, including adequate governance arrangements, periodic product reviews to ensure they remain fit for purpose and remuneration arrangements consistent with fair treatment of customers
- **Communications** – Closed-book customers should receive clear and timely communications about policy features at regular intervals and at key points in the product life cycle
- **Consideration of fund performance and policy values** – The firm should take steps to deal with poor fund performance on closed books, paying equal attention to closed and actively marketed products. Overall expenses should be allocated to closed books fairly, with cost allocations and actual customer outcomes regularly reviewed, and the reviews performed on a consistent basis. Closed book experience should be proactively monitored and used to consistently pass on benefits and costs to customers
- **Ease of exit** – Exit and paid-up costs should not be prohibitively expensive. Target ranges for with-profits payouts should be reasonable and payouts not vary too widely

Firms are expected to review their business practices within 3 months of the guidance being published, and make any changes they deem necessary.

2.7 Implementing information prompts in the annuity markets

The FCA has consulted on proposals to implement 'information prompts' for pension policyholders approaching retirement. The proposals require firms to deliver personalised information, in a prescribed format, including an information prompt that shows how much more annuity income could be available if an equivalent annuity is purchased elsewhere. Information on how to shop around must also be given.

The proposed information prompt will apply to all annuity sales and will be based on guaranteed quotes only. It is intended to form part of pre-sale disclosures. The FCA proposes that the same requirements will apply to non-written and online communications.

The consultation closed on 24 February 2017.

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2.8 Review of annuity sales practice

The FCA's thematic review of annuity sales practices examined the extent to which firms conducting non-advised sales have informed existing customers about the availability of, and their potential eligibility for, enhanced annuities (also known as impaired life annuities), and the fact that customers could potentially get a higher income from an enhanced annuity with another provider.

Although the FCA found no evidence of an industry-wide or systemic failure to provide customers with sufficient information about enhanced annuities through non-advised sales, it identified two types of non-compliance:

- **Type 1** – a failure of the process and therefore a breach of the rules
- **Type 2** – where the firm concluded that the type 1 failure was likely to have changed the customer's behaviour which may have caused an actual loss i.e. buying a standard instead of enhanced annuity or failing to shop around

The FCA found a relatively high incidence of type 1 failures across the firms in the sample, but customers generally received sufficient information to avoid a type 2 failure. However, a small number of firms did exhibit a high 'type 2' failure rate.

The thematic review has led to some firms having to review past sales and provide compensation to policyholders that should have been offered an enhanced annuity. This has been well publicised.

2.9 Regulatory reporting: Retirement income data

In November 2016 the FCA launched consultation paper CP16/36 on collecting retirement income data. The proposal is for providers of pensions, annuities and income drawdown products to complete two new regulatory returns:

- **REP015** – Retirement income flow data (every six months). This includes the type and volume of products sold, and through which distribution channels
- **REP016** – Retirement income stock data and withdrawals (annually). This includes the number of annuity contracts in payment, the value of assets under administration and details of withdrawals over the period

The consultation closed on 24 February 2017.

2.10 Professional indemnity insurance for general insurance intermediaries

The FCA has released a report on its thematic review of professional indemnity insurance for GI intermediaries. While there is no direct regulatory impact, it serves as a reminder that purchasers and providers of professional indemnity insurance should ensure their understanding of any cover in place is accurate. The review found that:

- In a small number of cases firms did not have the minimum cover required by the Prudential sourcebook for Mortgage and Home Finance Firms and Insurance Intermediaries (MIPRU)
- Some policies contained exclusion clauses which caused significant concern, as they could reduce effective cover below the MIPRU requirement
- There was a high level of inaccuracies in policies, with inadvertent gaps in coverage or inaccuracies which were apparently missed by both the firms/intermediaries purchasing the cover and the firms providing it
- There is sufficient breadth of cover available in the market
- Firms were generally able to obtain cover for a high level of indemnity

The FCA expects GI intermediaries not involved in the review to review their insurance policies to ensure they meet the requirements of MIPRU. Insurers which provide professional indemnity insurance in this area should review their products to ensure they meet the needs of their customers, including meeting the minimum cover level of MIPRU.

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3. Joint PRA and FCA activity

3.1 Authorisation and supervision of insurance special purpose vehicles

The PRA and FCA have jointly consulted on their proposed approach and expectations regarding the authorisation and supervision of insurance special purpose vehicles (ISPVs). The proposals are set out in the joint consultation PRA CP42/16 and FCA CP16/34. This should be read in conjunction with HM Treasury's consultation on regulations implementing a new regulatory and tax framework for Insurance Linked Securities.

The PRA will be responsible for granting authorisation for any entity wishing to operate as an ISPV in the United Kingdom. ISPVs will be dual-regulated by the PRA and FCA, with the PRA requiring the FCA's consent before granting approval.

The consultation closed on 23 February 2017.

4. FRC activity

4.1 Revision of Practice Note 20 and Withdrawal of Practice Note 24

The Financial Reporting Council ('FRC') issued revised Practice Note 20: The Audit of Insurers in the United Kingdom on 1 February 2017. The revisions allow for changes required to accommodate the PRA requirements regarding the audit of Solvency II information.

Practice Note 20 has also been revised to incorporate relevant material previously included in Practice Note 24: The Audit of Friendly Societies in the United Kingdom and Practice Note 24 is withdrawn.

4.2 Technical Actuarial Standards

The Financial Reporting Council ('FRC') has published new Technical Actuarial Standards (TASs). The new standards come into effect from 1 July 2017, replacing those currently in force, and must be complied with by all actuaries working within their scope.

5. European Commission activity

5.1 Key Information Documents

Making a strong bid for the least surprising regulatory development since the delays in implementing Solvency II is the European Commission's announcement that it has delayed the introduction of the key information document for packaged retail and insurance-based investment products (KIDs for PRIIPs) regulation until 1 January 2018. This decision was made following the rejection of the draft Regulatory Technical Standards (RTS) by the European Parliament in September.

After the Parliament's rejection of the RTS, the European Commission issued a letter to the European Supervisory Authorities (ESA) explaining its proposed changes to the draft RTS.

ESA has now published its response, which provides its opinion on the proposed changes to KIDs. The one issue raised by ESA is around the requirement to provide projections of future returns under different scenarios within the KID. ESA has questioned the European Commission's proposal to adjust the moderate scenario projection to have returns of 0 to reflect a more prudent approach, suggesting a mean of risk free returns would be a more appropriate rate to use.

6. EIOPA activity

6.1 Review of Standard Formula SCR

The European Insurance and Occupational Pensions Authority ('EIOPA') has launched a project dedicated to the review of the delegated regulation underlying Solvency II, and in particular the Solvency Capital Requirement (SCR) standard formula. Discussion paper EIOPA-CP-16/008 is the first step in the preparation of EIOPA's response to the Call for Advice received from the European Commission in July 2016 and will be followed by a number of round table meetings in 2017 before the final advice is submitted in February 2018.

The two mains goals are:

- To ensure a proportionate and technically consistent supervisory regime for (re)insurance undertakings
- To look for possible simplifications in the SCR standard formula and to ensure the proportionate application of the requirements

This is a detailed and wide-ranging consultation which could result in significant changes in how the SCR and risk margin are calculated. Responses were required by 3 March 2017.

6.2 Disclosure of information relating to transitional measures

In the run-up to Christmas, EIOPA published an opinion on the approach firms should use to disclose the linear reduction of the transitional measures to the firm's solvency position within the Solvency and Financial Condition Report (SFCR).

The short note explains that while the reduction in transitional measures should apply to 1 January each year, the SFCR (as at 31 December) should include all relevant information to present a transparent and relevant picture of the undertaking's solvency and financial position. EIOPA have therefore suggested that if the change to the transitional measures will have a "material impact" on the solvency position on 1 January of the next year, then this information should be disclosed within the SFCR from 31 December.

6.3 Limitations of regular supervisory reporting

EIOPA has published its first report on the use of limitations and exemptions from Solvency II regular supervisory reporting. Limitations are cases where National Competent Authorities (NCAs) permit undertakings to submit a reduced scope of quarterly reporting, such as the quarterly reporting waivers generally granted for PRA category 4 firms and below in the UK. These are allowed in cases where submission of the information would be overly burdensome to the undertaking, provided the information is reported at least annually. Undertakings can also be exempted from elements of both quarterly and annual reporting on an item-by-item basis, but all undertakings are expected to submit at least the Minimum Capital Requirement template on a quarterly basis.

The report is preliminary in nature, as annual submissions of the 2016 quantitative reporting will only be available from 2017 onwards, but provides details of the number of undertakings benefiting from limitations on the reporting received for the first quarter of 2016. It does not contain any information on the use of exemptions.

Out of the 3,111 undertakings across all member states, 924 are reporting limited quarterly information. This translates to 2.95% of the total technical provisions. The top three countries for number of undertakings with limitations are France, Luxembourg and the UK, which are also three of the largest markets. At present only eleven of the 31 NCAs have allowed limitations.

The report will be updated in 2017 to include full year limitations and any exemptions and this may (or then again may not) provide some more interesting information and trends.

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6.4 Recovery and resolution frameworks

In December 2016 EIOPA released discussion paper EIOPA-CP-16/009 on the potential harmonisation of recovery and resolution frameworks for insurers. This followed its survey of the existing frameworks in place across the EU and EEA earlier in 2016. The survey highlighted that:

- existing frameworks generally do not contain a requirement for the development of pre-emptive recovery and resolution plans;
- there was a mixed picture with regards to early intervention powers of member states' supervisory bodies; and
- a number of member states identified gaps and shortcomings within the existing frameworks.

EIOPA suggest within the paper that a harmonised environment should provide for minimum harmonisation only on the basis that this would benefit policyholders, the insurance sector and, more generally, financial stability in the EU.

Responses were required by 8 February 2017.

6.5 Methodology of risk-free interest rate term structures

EIOPA has released an update of the technical documentation of the methodology used to derive the risk-free interest rate term structures. The update relates to changes in the financial instruments used to derive the risk-free interest rates to reflect market developments.

6.6 Solvency II taxonomy roadmap

EIOPA has released a new taxonomy roadmap for 2017 onwards that will influence Solvency II quantitative reporting submissions. The roadmap suggests one planned change in taxonomy for the calendar year-end 2017.

6.7 EIOPA Q&As

EIOPA has published updated sets of questions and answers (Q&As) covering a range of Solvency II topics including:

- Guidelines on own risk and solvency assessment
- Guidelines on application of outwards reinsurance
- Guidelines on group solvency
- Guidelines on the loss-absorbing capacity of technical provisions and deferred taxes
- Guidelines on reporting and public disclosure
- Guidelines on reporting for financial stability purposes
- The final report on the ITS on procedures, formats and templates of the solvency and financial condition report
- Templates for the submission of information to the supervisory authorities
- Procedures, formats and templates of the solvency and financial condition report
- The allocation of credit assessments of external credit assessment institutions
- Symmetric adjustment of the equity capital charge

Firms should be aware that these Q&As are available here and are periodically updated.

7. UK legislation

7.1 Loss relief tax legislation

On 26 January 2017, Her Majesty's Treasury (HMT) published an update to the Finance Bill 2017 draft tax legislation. The draft legislation, originally published in December 2016 includes changes in respect of loss relief announced in the Budget 2016. The changes extend the range of profits against which brought forward losses can be offset but restrict the amount of profit that can be offset in any year.

The main loss relief changes are:

- Removal of restrictions that currently mean losses have to be offset against profits from similar taxable income streams
- Greater flexibility in being able to offset losses against profits in other group companies
- Loss relief restricted to 50% on any future profits in excess of £5m per annum per group

As well as affecting the revenue account, the changes may influence both deferred tax assets on the base balance sheet and the Solvency Capital Requirement (SCR) tax adjustment. Regardless of the potential financial impact, the changes will complicate the relevant calculations.

Although the Government recognises the detrimental impact on insurers of a potential reduction in deferred tax assets and/or the SCR tax adjustment, no special treatment will be given. Implementation is planned for April 2017.

7.2 Distributable profits

Changes to the Companies Act necessary to ensure Solvency II life insurers can continue to pay dividends became law on 30 December 2016. This change was needed as the original legislation depended upon the historical concept of the long-term business fund which does not exist under Solvency II.

7.3 Ogden Table discount rate review

The results of the Lord Chancellor's review of the discount rate used to calculate lump sum damages for future losses in personal injury and fatal accident cases (using the 'Ogden Tables') was announced late February 2017. The reduction in the rate from +2.5% per annum to -0.75% per annum has led to widespread publicity and significant increases in the potential cost of such claims to insurers.

Following the announcement, Lloyd's informed its Signing Actuaries and managing agents that it would be considering the impact of the rate change as part of assessing the margin in the Quarterly Monitoring Return Part C (QMC). Where Ogden is a material exposure Lloyd's expects the provisions included in the best estimate and assumptions underlying the valuation at particular rates to be clearly outlined, and any differences arising between Signing Actuary and Syndicate estimates due to consideration of the Ogden rate should be commented on in the report.

The revised rate comes into effect from 20 March 2017. However, a consultation on methodology has been announced and, therefore, it is uncertain as to how long the revised rate will apply.

7.4 Reforming the soft tissue injury (whiplash) claims process

In November the Ministry of Justice released its consultation paper on its proposals to tackle the high number and cost of personal injury claims. The paper outlines plans to:

- cap or remove altogether the amount an individual can claim for minor whiplash injuries (the suggested cap is £400, or £425 if there's a psychological element);
- introduce a clear tariff system of compensation claims with more significant injuries;
- raise the limit for cases in the small claims court for all personal injuries from £1,000 to £5,000; and
- ban offers to settle out of court without medical evidence – all claims would need a report from a MedCo accredited expert before any payout.

The consultation closed on 6 January 2017, with a response due to be published in April 2017.

Please contact your Barnett Waddingham consultant if you would like to discuss any of the above topics in more detail. Alternatively contact John Hoskin or Kim Durniat via the following:

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