Winter **2025**

Insurer Update

In this issue

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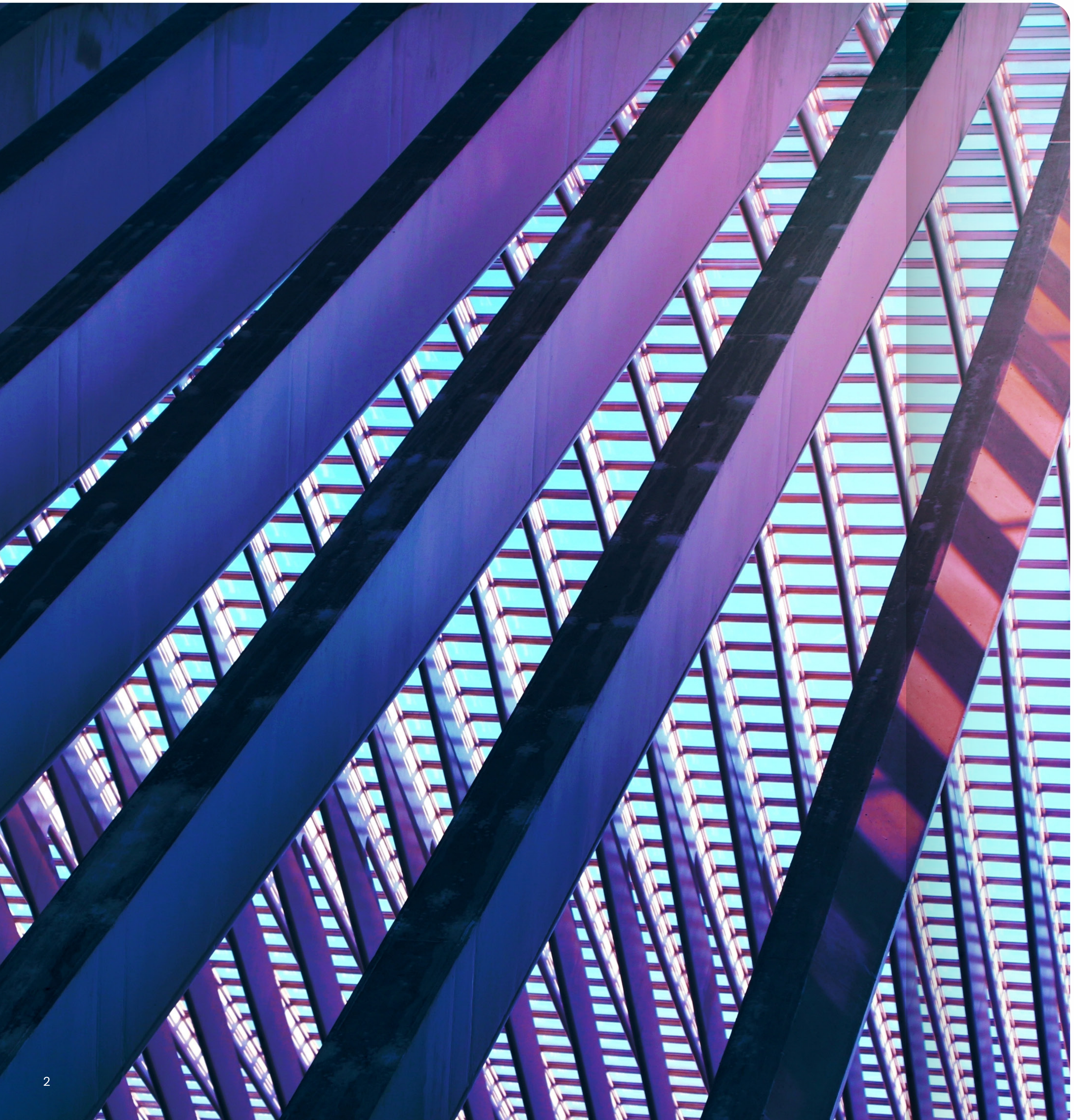

Insurer **Update** In this issue...

Welcome to our publication for **insurance carriers**

Welcome to our latest edition of Insurer Update. This publication aims to help carriers across the insurance market understand and digest some of the more pertinent financial reporting and tax developments, and highlight the implications for medium sized and smaller insurers.

How do our specialist PKF Global teams support motor insurers in Gibraltar? And what's the best way to prepare for next year's audit? Pauline Khong provides guidance for our clients and some top tips for the Rock's motor market.

The new Bermuda Corporate Income Tax will apply to multinational enterprises in scope of Pillar Two – so, does it affect you? Mimi Chan reviews the current situation, how this will impact UK intermediate entities and offers her advice.

Environmental and social governance continues to be a dynamic and evolving topic, always of interest to stakeholders. With the UK expected to endorse the International Sustainability Standards Board's IFRS S1 and IFRS S2 in the first quarter of this year, Jessica Wills examines the transition plan and explains how to ready yourself for sustainability reporting.

Since the UK's formal exit from the European Union in 2020, the Government has sought to adapt our financial services regulatory framework to reflect a post-Brexit position. James Randall reports on the PRA's final statement on Solvency II for insurance carriers, and how this will pave the way for the new Solvency UK.

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Focus on the Gibraltar market

How do our specialist teams support motor insurers on the Rock? And what's the best way to prepare for next year end's audit?

As a registered auditor of public interest entities (PIEs) in Gibraltar, we combine our expertise in actuarial, IT, regulation and auditing to serve numerous insurance companies in the territory, in addition to the UK and other jurisdictions.

GFSC and PRA/FCA alignment

There are 56 regulated insurance companies listed on the Gibraltar Financial Services Commission (GFSC) online register. Most are private limited companies authorised by the GFSC to conduct non-life insurance business (mainly motor) and carry out services in the UK.

So, the alignment of GFSC to UK regulatory standards makes good sense. For example, in Gibraltar the Solvency II regulation for the cost of capital rate has been amended to 4% in line with the Prudential Regulatory Authority (PRA) in the UK. The market rates to be used for discounting are not explicitly prescribed, but the GFSC considers the Bank of England's Sterling Overnight Index Average (SONIA) interest rates to be an appropriate benchmark.

SONIA effectively provides the overnight interest rates applied to bank transactions in the British sterling market. The GFSC is committed to being a credible regulator and playing a key part in the successful implementation of the Gibraltar Authorisation Regime (GAR).

We maintain regular dialogue with regulators in the UK and discuss with our Gibraltarian clients emerging developments.

Preparing for audit

So, how do our actuaries support their external audit colleagues with the review of GAAP/Solvency II (SII) reserves and solvency capital requirements (SCRs) for a motor client?

Our actuarial approach is typically a combination of independent re-projections for material segments or review of methodology and key assumptions. The chart below shows the areas we usually cover during our fieldwork. They're designed to assure the audit partner, as well as provide assurance to the Board, that the client booked reserves adequately reflect its risks and uncertainties.

An area which is often overlooked is disclosures regarding material judgements and estimations. For reserves, those can come from judgements in relation to whether to hold margins for uncertainty above best estimate and how that is done. In addition, companies should consider what the material sensitivities are – ie, being sensitive to assumptions or changes in methods that can drive a material change in the estimate. These need to be disclosed and explained in the notes to the financial statements, and will often require collaboration between finance and actuarial teams. But these disclosures will be of interest to your auditors and are also a hot topic for regulators.

Topical tips

Here are our actuaries' top four tips for the upcoming year end audit season:

1. Remember that calculating gross of reinsurance reserves matters too. Some of our clients focus mainly on net of reinsurance results. But both are important for the audited financial statements in the report and accounts. So don't forget to fully assess gross ultimate and earned claims, including IBNR, particularly for potential large losses. Then work out the potential recoveries that will mitigate those claims.

2. Ensure that any claims reserves for any life-changing personal injury cases that could potentially be lump sum settlements are based on the new Personal Injury Discount Rate (PIDR) of 0.5% that is effective from 11 January 2025.

3. Continue to monitor the impact of other external factors on the settlement of claims. These might include the recent Civil Liability Act reforms, credit hire arrangements, as well as the ongoing effects of changing inflation. We expect credit hire to continue to be a key element of claims costs. This is because vehicle repair time is longer, on average, after Brexit due to the delay in obtaining spare parts.

4. Provide rationale for applying EIOPA or SONIA market rates for calculating SII reserves until GFSC publishes formal guidance.

If you would like to discuss the topics raised in this article further, please contact Pauline Khong.

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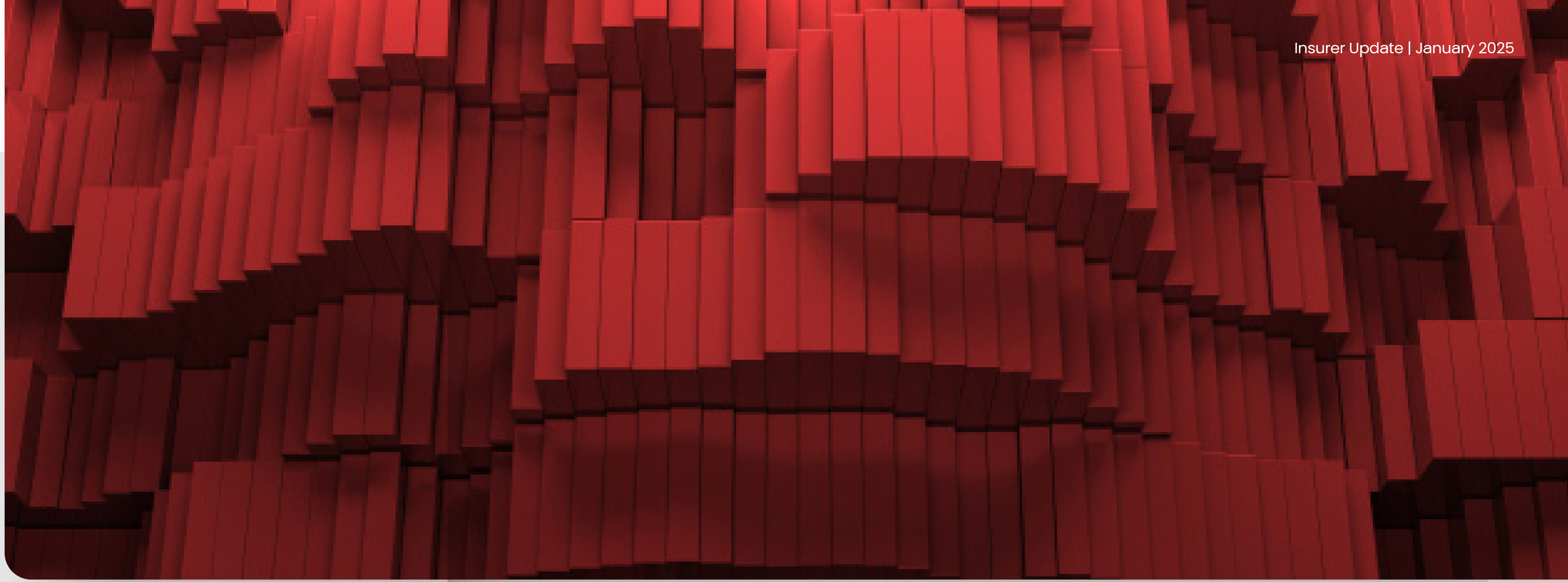

Bermuda corporate income tax (CIT): could it affect you?

The new Bermuda CIT will apply to multinational enterprises (MNEs) in scope of Pillar Two. How will this impact UK intermediate entities?

Bermuda is a global insurance and reinsurance hub, due to its robust regulatory framework and strong solvency regime. This means a number of (re)insurance groups are headquartered there.

This British overseas territory has never before imposed taxes on corporate income. The implementation of Pillar Two across various jurisdictions worldwide changes the picture. It opens up the possibility of an in-scope MNE's undertaxed Bermuda profits being taxed in another jurisdiction in which the MNE operates.

In response to this, Bermuda has introduced a corporate income tax (CIT) which applies specifically to Bermuda entities that are part of an MNE with annual revenue of €750m – ie, those in scope of Pillar Two. The rate of CIT has been set at 15% (in line with the Pillar Two minimum rate) and will apply from 1 January 2025. The effect of the CIT is to enable the territory to collect taxes on Bermuda income that could otherwise be collected by another jurisdiction under Pillar Two.

Bermuda is not itself implementing Pillar Two. Therefore, the administrative burden of making Pillar Two calculations and meeting its compliance obligations may fall to UK subsidiaries of Bermuda-headed MNEs if such subsidiaries are considered the intermediate parent entity.

What is the current situation?

CIT legislation was enacted in December 2023, and in August 2024, draft administrative provisions were shared for public consultation.

Further guidance is expected to be provided early in Q1 2025, but based on the responses to the consultation, it is likely that an in-scope entity will need to register for CIT as part of its annual filing of returns with the Registrar of Companies. Upon filing and declaration, two additional questions will need answering:

1. Is the company in scope of the CIT? If the answer is no, the entity must confirm why (by selecting from a provided list of responses)
2. If the answer to the above is yes, it must provide the details of a Bermuda tax resident company which will act as the "representative entity", ie be a point of contact (this can be the entity itself).

It is likely that an in-scope entity will need to:

- File a CIT return by the 15th day of the 10th month following the end of its financial year (eg, an entity with a 31 December 2025 year-end would need to file its return for that year by 15 October 2026; and
- Pay its CIT liability in two instalments during the financial year, with a final "top-up" payment (if needed) when the CIT return for that year falls due.

A number of elections are available that can override certain aspects of the core CIT rules. Companies have the option to make many of these elections now, or they can make these elections within their CIT returns.

The elections are broadly categorised as follows:

- **Annual elections** – once made, these can be revoked (or once revoked, they can be re-elected) at will from year to year.

  Example: the de minimis exemption, which mirrors the Pillar Two threshold test (in our **previous article**). This reduces an MNE's CIT liability to nil for a given year if both of these conditions are satisfied across its Bermuda group members:

  1. Average revenue is less than €10m
  2. Average net taxable income is less than €1m (or is a loss).

- **Five-year elections** – once made, these cannot be revoked (or once revoked, they cannot be re-elected) for a five-year period.

  Example: an election to determine the financial accounting net income or loss (FANIL) and starting point of the taxable income calculation, based on an approved financial accounting standard other than that used to prepare the ultimate parent entity's consolidated financial statements.

- **Other elections** – once made, these cannot be revoked at all.

  Example: an election to forgo the economic transition adjustment (ETA). The Bermuda CIT introduces an ETA which requires companies to calculate the tax basis of assets and liabilities based on their fair values at 30 September 2023 and determine an opening tax loss based on amounts generated after this date. If entities elect to forgo the ETA, companies instead calculate their opening tax loss based on net cumulative losses in the preceding five years.

Interaction with Pillar Two

CIT is a tax on profits, so it is a covered tax for Pillar Two purposes. This means it is included in the calculation of a Bermuda company's effective tax rate (ETR) under Pillar Two.

Certain elections, once made, might reduce a company's CIT liability in Bermuda and thereby the ETR in Bermuda. If the ETR in Bermuda is below the 15% minimum rate of tax, the MNE may need to pay a top-up tax for the difference in another jurisdiction. Bermuda won't collect the top-up tax itself, as it has not implemented Pillar Two.

What is our advice?

Care must be taken in deciding whether to make any of the Bermuda CIT elections. This process should include modelling the impact on the group's Pillar Two calculations.

If you would like further information or advice relating to the issues covered by this article, please contact Jannat Moyeen or Mimi Chan.

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Sustainability reporting: is your insurer ready?

ESG continues to be a dynamic and evolving topic, always of interest to stakeholders of insurers. We explore some of the key developments in the past year and how they might apply to your firm.

The UK is expected to endorse the International Sustainability Standards Board (ISSB)'s IFRS S1 and IFRS S2, in the first quarter of 2025. The creation of these two UK sustainability reporting standards (UK SRS) will contribute to a wider sustainability disclosure reporting framework led by the Treasury. This important step will improve the quality and consistency of sustainability reporting across the globe.

Once endorsed, following consultation, the FCA will be able to use the UK SRSs to introduce reporting and disclosure requirements for UK-listed firms. The Government will also decide, most likely in Q2 2025, on requirements for firms that do not fall within the FCA's regulatory net. But any changes would be effective no earlier than accounting periods beginning on or after 1 January 2026.

In the meantime, if you think your firm may be in scope, get familiar with IFRS S1 and S2. You may find some of our **previous articles** useful.

Transition plan disclosures and the FCA

The Transition Plan Taskforce (TPT) was formed in 2022 to establish the gold standard for transition plan disclosures. It published its voluntary disclosure framework in October 2023 and concluded its work in October 2024, with its materials and responsibilities transferred to the IFRS Foundation.

As part of the FCA's consultation on implementing UK SRS, it will also consult on strengthening expectations for transition plan disclosures relating to the TPT disclosure framework. This paves the way for enhanced disclosure and reporting on transition plans.

European sustainability standards

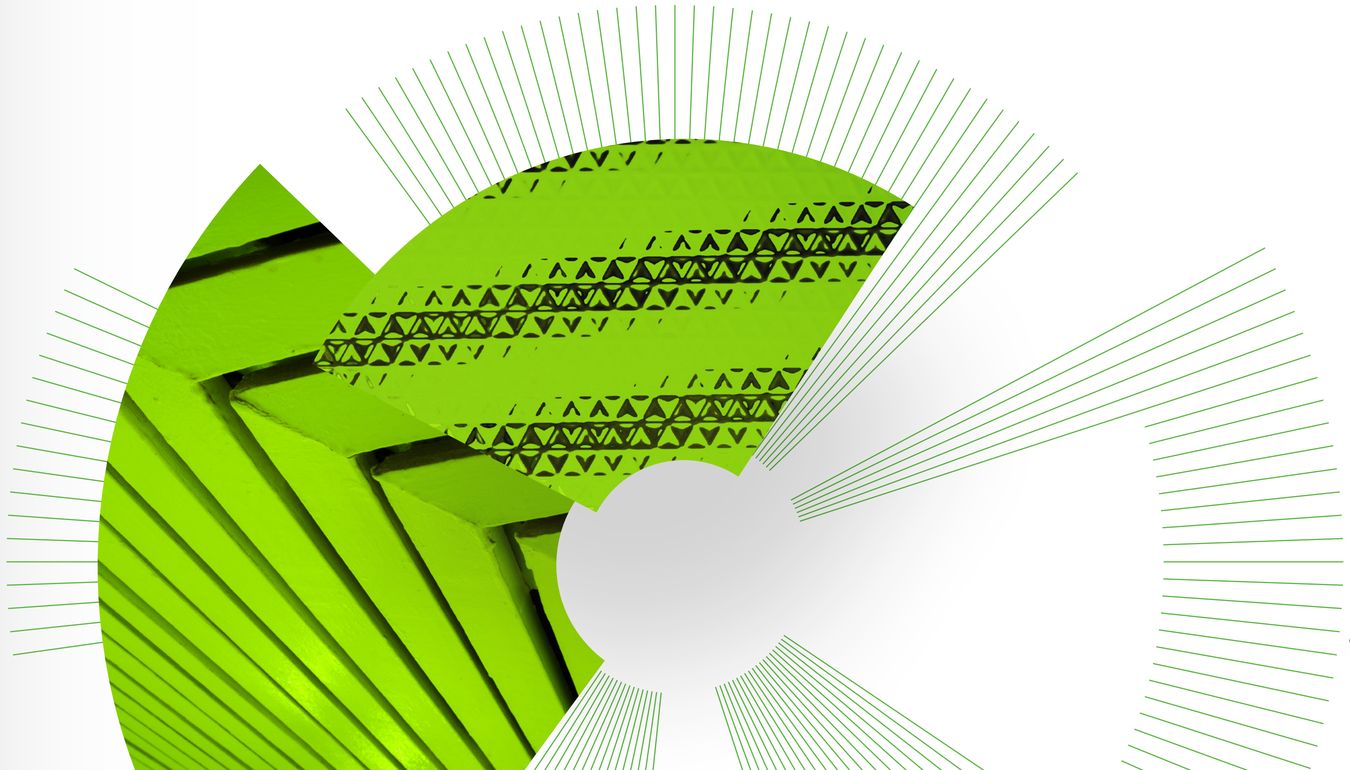
In Europe, meanwhile, new sustainability reporting requirements have been introduced through the Corporate Sustainability Reporting Directive (CSRD). Firms subject to the CSRD will have to report according to EFRAG's European Sustainability Reporting Standards (ESRS).

CSRD is being implemented in stages, with the first set of firms being asked to report in respect of the financial year commencing on or after 1 January 2024.

CSRD is notable for a number of reasons:

- It impacts a larger number and scope of firms, including non-EU firms and groups that meet certain criteria. This includes non-EU firms with debt or equity listed on an EU regulated market that need to report in respect of the financial year commencing on or after 1 January 2024
- Increased scope of the reporting requirements in accordance with ESRSs which cover environmental, social and governance topics – with a high number of data points and disclosure requirements
- Introduction of the double materiality concept. This requires firms to consider the effects of sustainability matters on the firm, and also the effects of the firm on society and the environment
- Mandatory requirement for limited assurance over the disclosures, with a limited assurance report forming part of the firm's annual report.

CSRD is complex and onerous, so impacted firms have a lot of work to prepare for and comply with the requirements. Over the coming years, CSRD will start to bite for more non-EU firms. So UK firms with subsidiaries, branches or significant activities in the EU should pay close attention. Please contact us if you need help assessing the impact of CSRD on your firm or require limited assurance over your CSRD reporting.



PRA developments

Since the publication of **Supervisory Statement 3/19** in April 2019, the PRA has retained its focus on insurers' management of the financial risks from climate change. This asks them to establish a strategic approach to climate-related financial risks by:

- Embedding consideration of such risks into governance arrangements
- Incorporating them into existing financial risk management practices
- Using scenario analysis to inform strategy setting and risk identification / assessment
- Developing an approach to making disclosures on the financial risks from climate change.

These requirements were reinforced in the **PRA's Insurance supervision: 2024 priorities letter** in January 2024. Although the regulator recognised that insurers have taken positive steps to embed their expectations, they felt further progress was needed. This particularly applies to scenario analysis and risk management. It will also be updating SS3/19 to provide clarity, for example on effective practices and wider regulatory developments and thinking, and to build on the SS3/19 approach.

Given this continuing focus, insurers should revisit their progress against SS3/19 expectations and be prepared for the expected update to help shape and refine their approach.

Lloyd's: insuring the transition

In July, Lloyd's published its **Insuring the transition roadmap v2.0** following a consultation at the end of 2023. It seeks to "build a marketplace which is resilient and responsive to the risks of today and innovating for the risks of tomorrow; a market that has the expertise and tools to support our clients as they transition, and a market which has the capital and strategy to grow and support more communities globally."

The roadmap clarifies:

- Lloyds' ambition to be the insurer of the transition
- How the Lloyd's oversight framework for the market will consider transition over the coming years.

It covers underwriting, investments, capital and reserving and portfolio risk management and provides a tool for managing agents for their sustainability strategies in these areas. All Lloyd's managing agents should review the roadmap, perform a gap analysis and develop their own action plan for addressing any omissions.

For more information about the matters raised in this article, please contact Jessica Wills.

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Solvency II: update for insurance carriers

Brexit meant changes to the regulatory landscape for finance. We report on the PRA's final statement on Solvency II, paving the way for the new Solvency UK.

Since the UK's formal exit from the European Union in 2020, the Government has sought to adapt the UK's financial services regulatory framework to this new position outside the EU.

This includes secondary objectives for the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) to facilitate the growth and international competitiveness of the UK economy, including the financial services sector. There is also a renewed focus on accountability to reflect the regulators' new responsibilities.

That has meant repealing certain legislation, which incorporated the Solvency II Directive in UK law, and replacing it with a new framework for regulating the insurance and reinsurance industry in the future.

In November, the PRA released its Review of **Solvency II: Restatement of assimilated law (PS15/24)**, which provides feedback on responses received to CP5/24 – and implements the conclusions of CP12/23 (Review of Solvency II: Adapting to the UK insurance market).

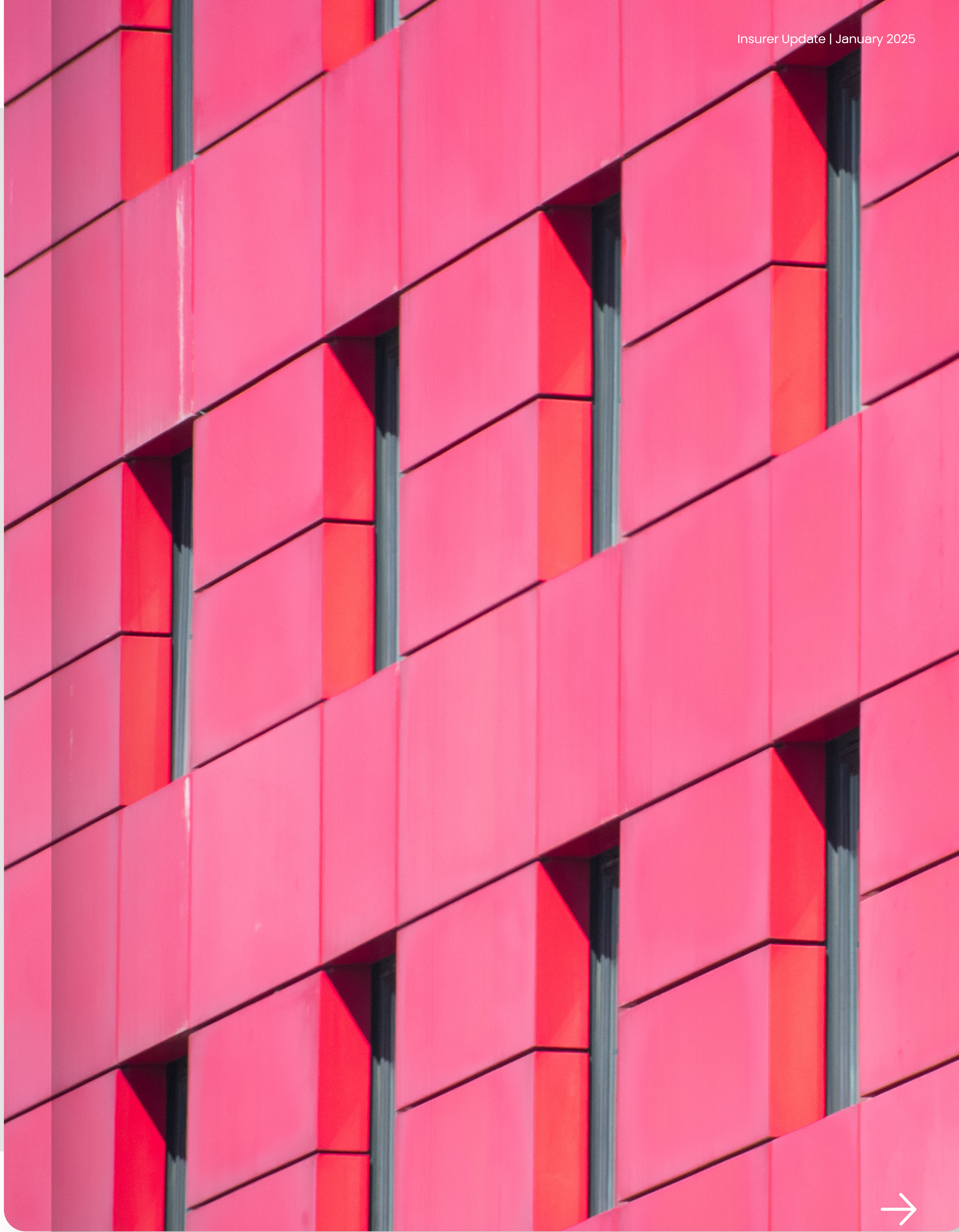
Bear in mind, also, that the near-final rules which we have discussed in **previous articles**, took effect from 31 December 2024. The policy statement represents the PRA's final explanation on the replacement of Solvency II assimilated law. It also further aligns the UK's prudential regime for insurers, inherited from the EU, with the UK framework under the Financial Services and Markets Act 2023.

This new regime will eventually be known as Solvency UK, once references to Solvency II are changed across all relevant policy materials.

What does it cover?

PS15/24 is detailed and wide-ranging. It's presented as follows:

- Chapter 1 – Overview
- Chapter 2 – General Provisions
- Chapter 3 – Technical Provisions: Risk Margin
- Chapter 4 – Technical Provisions: Further requirements
- Chapter 5 – Own funds
- Chapter 6 – Standard Formula Proposal 1: Restatement of assimilated law for the areas covered
- Chapter 7 – Standard Formula Proposal 2: Notifications and further use of section 138BA permissions
- Chapter 8 – Standard Formula Proposal 4: Definition of the term 'Ring-Fenced-Fund'
- Chapter 9 – Systems of governance
- Chapter 10 – Public Disclosure
- Chapter 11 – Insurance Special Purpose Vehicles
- Chapter 12 – Insurance Groups
- Chapter 13 – Other proposals in CP5/24
- Chapter 14 – General points raised by respondents
- Chapter 15 – Other minor amendments to PRA rules, reporting templates and instructions and policy material.



Who is the policy statement targeting?

Stakeholders are UK Solvency II firms and UK insurance undertakings. This includes current non-directive firms (those outside the scope of UK Solvency II), those intending to provide insurance services in the UK in the future and those who may wish to become non-directive firms from 31 December 2024.

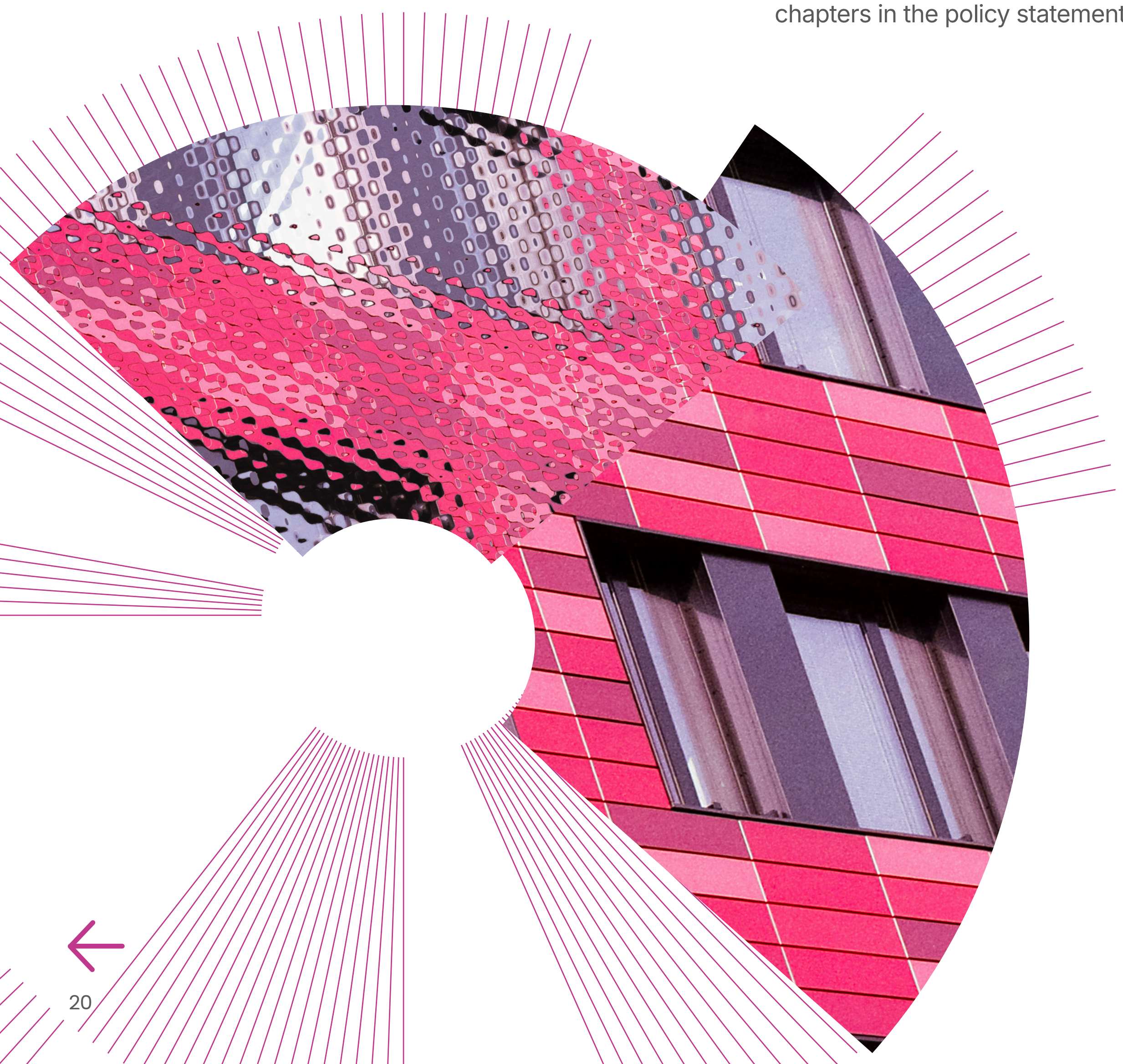
To help these stakeholders, there are also several Appendices. These include a full set of mapping tables in Appendix 8, outlining the restatements of Solvency II assimilated law into the PRA framework.

Important proposals

As well as the restatements to assimilated law, CP5/24 set out two significant proposals. Firstly, the new time-limited transitional rule in the Own Funds part of the PRA Rulebook. This essentially classifies legacy paid-in preference shares issued before 18 January 2015 as irrelevant, for a period of 25 years. Secondly, the restatement of amounts denominated in EUR into GBP using the conversion rate set out in PS2/24.

Responses to CP5/24 were largely supportive. There was little additional cost or burden for firms, given that its primary function was the restatement of existing requirements. Where policy changes were proposed, respondents saw these as sensible and non-contentious. The proposals and mapping tables were seen as providing greater clarity to requirements placed on firms.

But there were requests for further guidance on the Standard Formula Proposals 1, 2 and 4, so these have been given individual chapters in the policy statement.



Do the final rules differ from the consultation?

There are two cases where the final rules differ significantly from CP5/24. On the loss-absorbing capacity of deferred taxes (LACDT) under the SF, there is a new transitional rule. This delays the PRA permission requirements to recognise future taxable profits (FTP) in the LADCT calculation until 30 December 2025. So, it's important to comply with this transitional rule to benefit from FTP in the LACDT calculation.

The other difference is on amendments to the proposed ring-fenced fund (RFF) definition so as to maintain the PRA's current policy approach to RFFs. These amendments preserve the link to 'restricted own funds' and explicitly exclude MA portfolios from the definition.

In a raft of Solvency II prudential regulation releases, PS15/24 was also accompanied by:

- Supervisory statements on the calculation of technical provisions and treatment of pension scheme risks
- Policy statements on volatility adjustment permissions, approach to insurance own funds permissions, and approach to standard formula adaptations
- A further consultation paper on proposed changes to the UK Insurance Special Purpose Vehicles regulatory framework.

So, none of the information contained in PS15/24 should come as a huge surprise to UK insurers. But it does provide some welcome clarity as we embark upon the 31 December 2024 reporting season, as well as a clear direction of travel.

For more information on Solvency II, please contact James Randall or Martin Watson.

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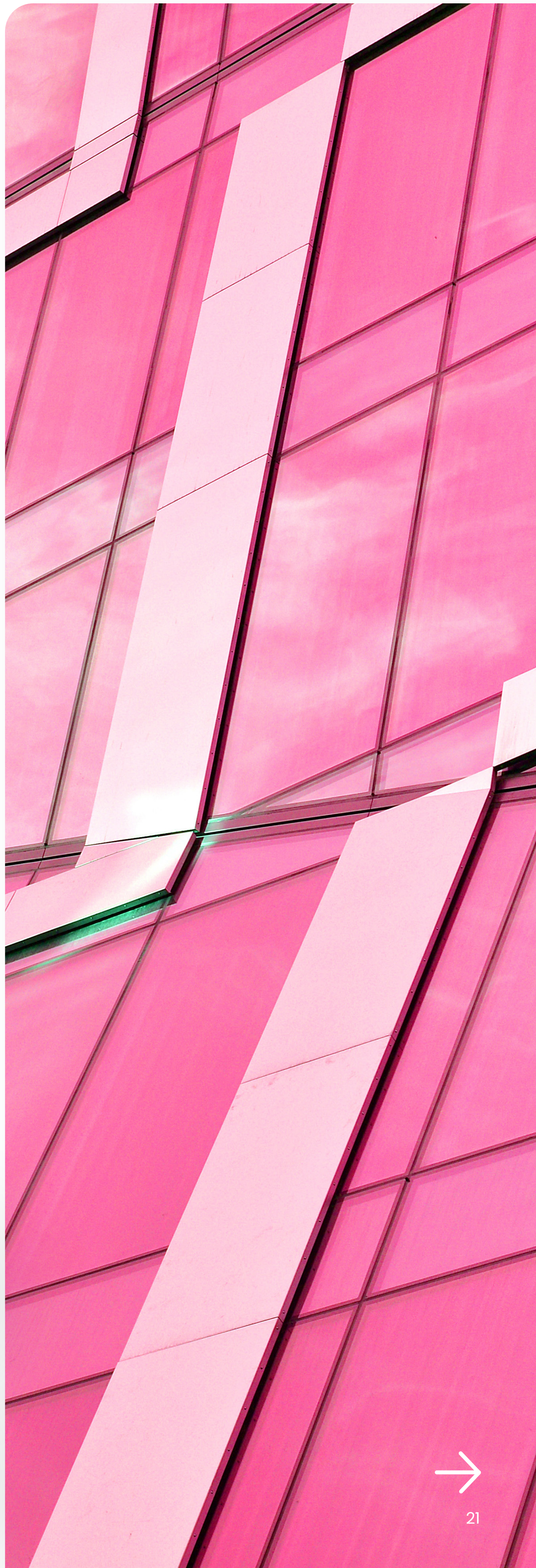

About PKF

Simplifying complexity for our clients

PKF is one of the UK's largest and most successful accountancy brands.

We have been a trusted adviser to the UK insurance industry for over 150 years and have one of the largest and most experienced teams of insurance experts within the accountancy profession.

Established initially as a Lloyd's practice, our clients now span the entire insurance market – from Lloyd's syndicates to life, general and health insurers, brokers and MGAs.

Our expert Insurance team are specialists in dealing with clients who operate across borders and that team extends to include colleagues in Insurance hubs including, Gibraltar, Malta, Guernsey, the US and Ireland.

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1,450+ Employees and 180 partners	**150+** Insurance specialist staff & partners	**$1.4bn+** In aggregate fee income
£202m Fee income and growing rapidly	**30%** Advisor to one third of the UK's Top 50 Brokers	**21,000** Employees

Get in touch today

To see how we can help...

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