

Being better informed

FS regulatory bulletin

FS regulatory insights

July 2023

In this month's edition:

- PRA consults on Solvency II reforms
- BoE launches system-wide exploratory scenario exercise
- PSR confirms plans for banks to reimburse APP scam victims
- EU reaches agreement on CRR3/CRD6 package



Executive summary



Welcome to this edition of 'Being better informed', our monthly FS regulatory bulletin, which aims to keep you up to speed with significant developments and their implications across all the financial services sectors.



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Regulators and policymakers were busy in the run up to the end of June, with the Financial Services and Markets Bill completing its passage through Parliament, receiving Royal Assent to become the Financial Services and Markets Act 2023 (FSMA 2023). The Act delivers fundamental changes to the UK's regulatory architecture, and implements a suite of policy changes. The passage of the Bill will kick start a multi-year process of repealing and reforming UK onshored regulation, and will trigger a number of FCA and PRA consultations on specific policy areas, such as on wholesale markets reform.

The PRA published its much-anticipated consultation on reforms to Solvency II. The PRA set out a range of measures designed to remove certain onerous requirements, give insurers greater flexibility, encourage entry, and increase competitiveness. The reforms will require secondary legislation to be laid by the Government, and HM Treasury (HMT) published two draft statutory instruments, outlining changes to the risk margin, matching adjustment and fundamental spread calculations. Some reforms are expected to be implemented by the end of this year, and the remainder in 2024. See our [Hot Topic](#) for more details. The PRA is due to consult in September 2023 on reforms for life insurers relating to investment flexibility and the matching adjustment.

Also of interest to life insurers is the PRA's letter to Chief Risk Officers, sharing feedback on its review into funded reinsurance (FundedRe) arrangements. The PRA has previously warned insurers in the bulk purchase annuity (BPA) market, noting their increased reliance on FundedRe to support BPA business.

The PRA's review found shortcomings relating to the structuring of FundedRe transactions,

corresponding risk management frameworks, and how the transactions are reflected in capital requirements. The PRA asks life insurers to consider its findings and take any necessary remedial steps. Our [At a glance](#) publication provides more information.

Elsewhere, the Bank of England (BoE) published details of its system-wide exploratory scenario (SWES), the first exercise of its kind to understand market-wide dynamics. The BoE is seeking to understand the behaviour of banks and non-bank financial institutions in market stress situations, and how this might impact UK financial stability. The SWES exercise will cover a sample set of firms, including banks, insurers, central counterparties and funds. The BoE will publish full details of the stress scenario later this year, and publish a final report in 2024, outlining the system-wide findings and its assessment of risks to SWES 'markets of focus' and wider UK financial stability. Please see our [At a glance](#) briefing for more information.

Outside the UK, the European Council and European Parliament reached political agreement on the CRR3/CRD6 package, which will implement the Basel 3.1 package into EU legislation. The outstanding items in the agreement included the output floor, ESG, treatment of cryptoassets, fit and proper assessment, and the third country regime. Third country banks will be prevented from serving clients in many cases on a cross-border basis. Existing third country branches in the EU will also be subject to a number of new regulatory requirements, including reauthorisation. Overall, the EU's approach to implementation has modified the original Basel 3.1 standards and is likely to mean significant differences in approach between the UK and EU.

Finally, the Payment Systems Regulator (PSR) confirmed it is taking forward plans to require payment service providers (PSPs) to reimburse authorised push payment (APP) fraud losses in all but exceptional cases. The PSR is broadly taking forward the proposals consulted on in September 2022, requiring mandatory reimbursement of consumers for all types of APP scams, except in cases of first party fraud or gross negligence (the latter does not apply if the victim is a vulnerable consumer). The costs of reimbursement will be shared equally between sending and receiving PSPs. The standards will replace the voluntary Contingent Reimbursement Model Code, and will require firms to go further to prevent APP fraud and change customer behaviour, and to deliver faster reimbursement processes. The new requirements will come into force in 2024. Our [At a glance](#) publication provides further analysis.

Read on to find out more about these and other developments in this edition of Being better informed. You can also visit our PwC [webpage](#) for further regulatory insights, including our podcast [episode](#) on how firms can prepare for the EU's Corporate Sustainability Reporting Directive, our [blog](#) on the impact of the recently signed Memorandum of Understanding on financial services cooperation between UK and EU, and our [Reflections](#) article which examines the increasingly critical role of stress testing in building financial resilience.

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Contents

How to read this bulletin?

Review the Table of Contents and the relevant Sector sections to identify the news of interest. We recommend you go directly to the topic/article of interest by clicking in the [active links](#) within the table of contents.

Executive summary	2
Cross sector announcements	4
Banking and capital markets	6
Asset management	9
Insurance	10
Contacts	12

Cross sector announcements

In this section:

Conduct	4
Cryptoassets	4
Financial stability	5
Regulatory framework	5
Sustainability	5



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Conduct

FCA issues readiness questions for Consumer Duty

With almost one month to go until the Consumer Duty implementation deadline for new products and services, on 28 June 2023 the FCA [published](#) ten key questions that firms should ask themselves to make sure they are on track to meet the deadline.

The questions emphasise the FCA's expectations for firms to evidence the tangible actions they have taken to prepare for the Duty. For example, the questions ask what changes firms have made to the design of products and services, and how they are acting on the results of communications testing. The questions also focus on customer services and support, with the FCA asking how firms have satisfied themselves that the quality and availability of post-sale support is as good as pre-sale support.

The FCA reminds firms that it expects boards, or equivalent management bodies, to have clear oversight of implementation plans and that firms should have identified any potential gaps or weaknesses in their compliance and developed plans to remedy this. The FCA notes firms should expect to be asked these questions in their interactions with the regulator in the lead up to the 31 July 2023 implementation deadline and beyond.

FCA proposes Handbook clarifications

The FCA issued a consultation on minor changes to its Handbook, in [Quarterly Consultation No 40](#) on 2 June 2023. It proposes: corrections and clarifications to MIFIDPRU 7 and SUP 16, introducing a post-trade transparency deferral for exchange traded fund transactions executed at net asset value, and clarifying the scope of the ban on offering retail clients incentives to invest

in high-risk investments (as outlined in [PS22/10](#) in August 2022). The consultation closed on 10 July 2023.

Cryptoassets

FCA publishes promotion rules for cryptoassets

The FCA set out its final policy position and near-final Handbook rules for the financial promotion of cryptoassets in a [policy statement](#) on 8 June 2023. The near-final rules have been approved by the FCA Board, with final rules expected shortly and set to take effect from 8 October 2023.

The publication confirms the FCA's approach to categorise cryptoassets as 'Restricted Mass Market Investments', meaning cryptoassets will be able to be mass marketed to consumers, but subject to certain restrictions.

These restrictions include the need for financial promotions to include clear risk warnings (in particular highlighting the lack of FSCS and FOS protection), a ban on incentives to invest (including 'refer a friend' incentives), and client categorisation and appropriateness assessment requirements. The policy statement was accompanied by a [guidance consultation](#) to support firms' understanding of the implications of the new rules for cryptoasset promotions.

The final rules for cryptoassets align with the FCA's financial promotion rules for high risk investments [confirmed in August 2022](#). These rules initially excluded cryptoassets until relevant legislation had been made and the FCA had considered whether a more bespoke approach for cryptoassets was necessary. The FCA has shortened the implementation timeline for the new rules from six to four months, meaning firms intending to market cryptoassets to UK consumers will have until 8 October 2023 to comply.

Financial stability

BoE outlines resilience measures for LDIs

The Bank of England Executive Director for Financial Stability, Sarah Breeden, made a speech [published](#) on 16 June 2023, setting out the range of new measures the Financial Policy Committee (FPC) is developing to build resilience within Liability Driven Investment (LDI) funds, and how these might support greater resilience in non-bank financial institutions. Breeden explained that the FPC has recommended a framework for steady-state resilience in LDIs, including measures to prevent forced deleveraging and gilt sales.

Regulatory framework

Financial Services and Markets Bill receives Royal Assent

The Financial Services and Markets Bill gained Royal Assent on 29 June 2023, becoming the Financial Services and Markets Act 2023. The Act implements the UK's post-Brexit regulatory framework, repealing retained EU law from the statute book and delegating financial services rule-making powers to the regulators. HMT and regulators will now commence the phased process of repealing retained EU legislation and preparing relevant rule review consultations on specific areas of regulation.

PRA sets out approach to rules review

The PRA [published](#) Consultation Paper (CP)11/23 on 30 June 2023, setting out its proposed approach to reviewing its rules, as required by the Financial Services and Markets Act 2023. The PRA had previously [published](#) Discussion Paper (DP)4/22, which set out the PRA's intended future approach to policymaking. The consultation closes on 29 September 2023 and the PRA will then publish a Policy Statement confirming its final approach.

The PRA's proposed framework for rule review consists of four main elements: regular monitoring of indications that rules may need to be reviewed; prioritisation and selection of rules to be reviewed; determination of the review method and timing;

and execution of the review findings (including changes to the PRA Rulebook where applicable).

The PRA is also proposing to engage with stakeholders on its rule reviews, through existing channels (such as consultations and supervisory engagement), relevant panels (such as the PRA Practitioner Panel), and new engagement channels specifically set up to support rule reviews. The PRA is also proposing to create a public webpage dedicated to its rule review activities, to support transparency.

Sustainability

European Supervisory Authorities update on greenwashing risks

The European Supervisory Authorities (ESAs) published on 1 June 2023 their progress reports on greenwashing, in response to a request from the European Commission. The ESAs published a common high-level definition of greenwashing: "a practice where sustainability-related statements, declarations, actions, or communications do not clearly and fairly reflect the underlying sustainability profile of an entity, a financial product, or financial services. This practice may be misleading to consumers, investors, or other market participants". Each ESA - [European Banking Authority \(EBA\)](#), [European Insurance and Occupational Pensions Authority \(EIOPA\)](#) and [European Securities and Markets Authority \(ESMA\)](#) - published a report looking at greenwashing risks within their remits. Key findings include:

- EBA: The greatest greenwashing risk lies in pledges about future ESG performance. Examples of greenwashing are mostly at entity level not product level, except for investment products. The risks associated with greenwashing, such as reputational and operational risks, are also considered.
- ESMA: Assess which areas of the sustainable investment value chain are more exposed to greenwashing risks (e.g. misleading sustainability claims), underlying drivers and transmission channels (e.g. for greenwashing-related

financial risks). Preliminary remediation actions are also included.

- EIOPA: Greenwashing risks relate largely to misleading claims (e.g. that mislead consumers and damage firms' reputations) and can occur to varying degrees as part of a broader set of conduct risks at all lifecycle states in insurance and pensions.

The ESAs intend to publish their final reports on greenwashing - including final policy recommendations - in May 2024.

Banking and capital markets

In this section:

Compensation schemes	6
Conduct	6
Financial crime	7
Financial stability	7
Recovery and resolution	7
Technology	7



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Compensation schemes

PRA confirms proposals on depositor protection

The PRA [published](#) Policy Statement (PS)7/23 on 30 June 2023, confirming amendments to the UK deposit protection framework to ensure that the rules remain relevant and costs to firms are proportionate to the regulatory benefits. The PRA had previously [published](#) Consultation Paper (CP)9/22, setting out proposals to amend the Depositor Protection (DP) Part of the PRA Rulebook, delete the DAS Part of the PRA rulebook, and make minor amendments to PRA SS18/15 'Depositor and dormant account protection', the PRA's Statement of Policy on 'Deposit Guarantee Schemes', and the PRA's Statement of Policy on 'Calculating Risk-Based Levies for the Financial Services Compensation Scheme (FSCS) deposits class'.

The PRA [published](#) PS10/22 on 28 November 2022, confirming other proposals set out in CP9/22. In PS7/23, the PRA is confirming rule amendments covering the holding of monies by a trust that come within the scope of the temporary high balance regime; clarifying that depositors of firms that have their Part 4A permission removed will not benefit from the FSCS; providing despositors with a right of withdrawal in the event that a bank restructuring results in a reduction in FSCS protection; and confirming that the annual FSCS notification requirement for depositors does not apply to depositors that are not entitled to FSCS protection. The amendments came into force on 1 July 2023.

Conduct

FCA makes changes to implement Mortgage Charter

The FCA issued policy statement [PS23/8](#) on 30 June 2023, which makes changes to its Mortgages and Home Finance: Conduct of Business (MCOB) sourcebook to support the implementation of the Government's [Mortgage Charter](#). UK mortgage lenders and the FCA agreed on 23 June 2023 to implement a Mortgage Charter of measures to support borrowers facing higher remortgage costs due to increased interest rates.

The FCA is making changes to its responsible lending rules (MCOB 11.6), without consultation. The changes will enable firms to allow mortgage borrowers to:

- reduce their capital repayments (including to zero, and paying interest only) for up to six months
- fully or partly reverse a term extension within six months of extending the term.

Both options may now be offered without a new affordability assessment. The regulator stresses these are limited exemptions from its affordability requirements. Lenders still need to assess affordability if a borrower wants to permanently convert to an interest-only mortgage or extend the term beyond their expected retirement date.

The FCA says firms will need to ensure customers are provided with sufficient information to support their decision, including making clear the potential risks and costs of changing a mortgage contract. The rule changes take effect immediately.

As part of its supervisory activity, the FCA plans to request data to assess how firms are making

use of the changes, and the outcomes for customers. It intends to review the changes in a year's time.

The 32 lenders which signed the Charter have also agreed to several other measures, including that no borrowers will be forced to leave their home unless in exceptional circumstances, within a year of first missing a mortgage payment.

FCA to require banks to explain savings rates

The Chancellor met with CEOs of regulators, including Nikhil Rathi of the FCA, on 28 June 2023, to agree a range of measures to support consumers with the rising cost of living. In financial services the focus was on savings rates. The FCA [agreed](#) to require the largest banks and building societies to explain the pace and extent of their pass through of interest rates, and how they are proactively supporting savers to switch to high interest rate products.

Financial crime

PSR confirms APP reimbursement plans for banks

The Payment Systems Regulator (PSR) published a [policy statement](#) on 7 June 2023, confirming it is taking forward plans to require payment service providers (PSPs) to reimburse authorised push payment (APP) fraud losses in all but exceptional cases. The requirements will apply to all PSPs which send and receive Faster Payments in the UK, including retail banks and building societies. They come after PSR consultations in [November 2021](#) and [September 2022](#), and are part of the Financial Services and Markets Bill reforms.

The PSR is broadly taking forward the proposals as consulted on, requiring mandatory reimbursement of consumers for all types of APP scams, except in cases of first party fraud or gross negligence (the latter does not apply if the victim is a vulnerable consumer). It intends to publish guidance on what gross negligence means in practice, in Q3 2023. The costs of reimbursement are to be shared equally between sending and receiving PSPs.

The PSR is making some changes to the proposals as consulted on: it is removing the £100 minimum threshold for claims, will consult on a maximum level of reimbursement in Q4 2023, and is extending the time limit for PSPs to reimburse fraud victims from 48 hours to five business days.

The requirements will come into force in 2024. The PSR will consult on a specific start date in Q3 2023, and publish a final date alongside the final legal instruments in Q4 2023. It expects industry to start work now to implement the requirements.

The standards will replace the voluntary Contingent Reimbursement Model Code. The PSR's ambition is for around 95% of losses to be reimbursed under the new requirements (compared to around 59% currently).

See our [At a glance](#) publication for further details.

Financial stability

BoE launches system-wide exploratory scenario exercise

The Bank of England (BoE) [published](#) details of its system-wide exploratory scenario (SWES) on 19 June 2023, which is the first exercise of its kind to understand market-wide dynamics. The BoE is seeking to understand the behaviour of banks and non-bank financial institutions (NBFIs) in market stress situations, and how this might impact on UK financial stability.

The SWES exercise will cover a sample set of firms, including banks, insurers, central counterparties and funds (pension funds, hedge funds, asset management funds). The BoE will publish the full list of participants and details of the stress scenario later in 2023. It will then publish a final report in 2024, outlining the system-wide findings and its assessment of risks to SWES 'markets of focus' and wider UK financial stability reforms.

See our [At a glance](#) publication for more details.

Recovery and resolution

PRA sets out solvent exit planning regime

The PRA [published](#) CP10/23 on 28 June 2023, setting out its proposals for non-systemic banks and building societies to prepare for (and if necessary execute) an orderly solvent exit. The proposals cover new rules and supervisory expectations for firms' preparations for a solvent exit as part of their business-as-usual activity; new supervisory expectations for how firms should prepare for and manage a solvent exit execution plan; and changes to [Supervisory Statement \(SS\)3/21](#) ('Non-systemic UK banks: The Prudential Regulation Authority's approach to new and growing banks') as well as a [new Supervisory Statement](#) ('Solvent exit planning for non-systemic banks and building societies').

In-scope firms would be expected to produce and document a solvent exit analysis. They would also be expected to prepare a solvent exit execution plan in the event that a solvent exit became a realistic scenario, as well as monitoring and managing its solvent exit. The PRA expects its proposals to improve the likelihood of firms successfully executing a solvent exit.

Firms would also be expected to produce a solvent exit execution plan, once they began to consider a solvent exit option or if the PRA informed the firm that it should prepare for a solvent exit. The PRA expects firms' solvent exit plans to cover specified topics, including an outline of the firm's solvent exit actions and indicators; potential barriers and risks; resources and costs; communication; governance and decision making; and assurance. The PRA states that the level of detail in the solvent exit analysis should be proportionate to the nature, scale and complexity of the firm.

The consultation closes on 27 October 2023, and the PRA plans to implement the proposals in Q3 2025.

See our [At a glance](#) publication for further details.

Technology

JROC takes forward next phase of open banking

The Joint Regulatory Oversight Committee (JROC) unveiled a new work programme to advance [recommendations](#) for the next phase of open banking, in a [press release](#) published on 6 June 2023.

The JROC launched two new working groups:

- Variable Recurring Payments (VRP) Working Group: this will devise a blueprint for the phased roll-out of non-sweeping VRP, with completion anticipated by the end of September 2023.
- Future Entity Working Group: this group will consider the design, role, structure, and funding of the future open banking entity. The working group will present its findings to the JROC by the end of September 2023, with the JROC set to publish its views in a subsequent update towards the end of 2023.

The VRP Working Group will operate under the leadership of the Payment Systems Regulator, while the Future Entity Working Group will be chaired by the FCA.

In addition to the new working groups, Open Banking Limited (OBL), the open banking implementation entity, has been tasked by the JROC to lead and coordinate work on four key themes:

- levelling up availability and performance
- mitigating the risks of financial crime
- developing proposals for dispute processes
- improving information flows to third party providers and end users.

The JROC has outlined specific tasks for the OBL, which include a potential collaboration with Pay.UK. OBL will provide monthly updates to the JROC on the progress of these initiatives, accompanied by a detailed timeline for completion.

Open banking committee sets out principles for commercial APIs

The Joint Regulatory Oversight Committee (JROC) set out five principles to guide the development of premium application programming interfaces (APIs) in a [paper](#) published on 26 June 2023. These principles are integral to JROC's [roadmap](#) for the subsequent phase of open banking in the UK.

The paper describes the features of a secure, sustainable commercial model for premium APIs. This strategy is designed to ensure that the prices that banks and other payment service providers charge third-party providers for open banking services are competitive and fair. JROC aims to promote continuous development and innovation in a manner that is safe and effectively mitigates cyber and financial crime.

The JROC sets out that fees and charges for premium APIs should:

- broadly reflect relevant long run costs of providing premium APIs
- incentivise investment and innovation in premium APIs
- incentivise take up of open banking by consumers and businesses and use of network effects
- treat third-party providers fairly
- be transparent.

Industry participants now need to agree commercial models for premium APIs that are sustainable, safe and scalable. These principles should guide the advancement of these commercial frameworks, the piloting of commercial models, and the testing of new premium APIs. Premium APIs will need to facilitate all types of open banking-enabled products and services.

Asset management

Conduct

9



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Conduct

FCA expands retail access to long-term asset funds

The FCA published a [policy statement \(PS23/7\)](#) on 29 June 2023 which sets out new rules regarding Long Term Asset Funds (LTAFs). LTAFs are a new type of open-ended authorised fund specifically designed to invest efficiently into long-term, illiquid assets. As a result of the new rules, LTAFs will be recategorised from a Non-Mass Market Investment to a Restricted Mass Market Investment. This means that more mass market retail investors, self-select defined contribution pension schemes and Self-Invested Personal Pensions will be able to access and invest into an LTAF. Changes include: amending the risk warning/summary text, setting fund-of-funds exposure limits, modifying third-party valuation rules, and amending retail investor protection rules.

The new rules will come into force on 3 July 2023. There will be a transitional period for authorised fund managers which already have funds authorised as LTAFs, of up to one year.

As the safeguards of the regimes for high-risk investments have been applied to LTAFs, the FCA is also asking for views on whether Financial Services Compensation Scheme coverage for LTAFs should be removed or whether any other actions should be considered. Views are requested by 10 August 2023.

Insurance

In this section:

Capital and liquidity

10



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Capital and liquidity

PRA identifies shortcomings in funded reinsurance arrangements

The PRA issued a [letter](#) to the Chief Risk Officers of life insurers on 15 June 2023, sharing feedback on its review into funded reinsurance (FundedRe) arrangements. The PRA carried out its review to enhance its understanding of counterparty risks arising from FundedRe, given the increasing reliance by insurers on FundedRe to support bulk purchase annuity portfolios.

The PRA identifies four risks: 1) probability of recapture (PR) given historical evidence of default risk might not address recapture risk, 2) correlated PR increases the likelihood that credit cycle shocks affect multiple reinsurers simultaneously, 3) loss given recapture as a credit cycle shock is likely to cause the deterioration of the reinsurer at the same time as the collateral portfolio, and 4) certain management actions may be ineffective on recapture.

The PRA notes that certain structural features of FundedRe transactions create the risk that firms recapture sub-optimal portfolios with unmatched or with inadequate assets, and with limited ability to be transformed effectively to the firms' preferred portfolio. The PRA also finds that risk frameworks and internal models need to be more closely connected to the terms of the FundedRe contracts, and that there is overreliance on management actions under times of stress which may not be viable in all market conditions.

The PRA states life insurers should consider its findings and take remedial steps as necessary. The PRA also states it is considering the need for further policy proposals in this area. Lastly, the PRA instructs all insurers to inform their PRA supervisors promptly of material FundedRe transactions entered into from 15 June 2023.

See our [At a glance](#) publication for more details.

HMT proposes changes to risk margin and matching adjustment

HMT published two [draft statutory instruments \(SIs\)](#) on 22 June 2023, for implementing changes to the prudential regime for insurers. The SIs outline changes to the risk margin (RM), matching adjustment (MA) and fundamental spread (FS) calculations.

The draft SIs propose a new methodology for calculating the risk margin using a 'risk tapering' (also known as the 'lambda') approach. In addition, the cost-of-capital rate for calculating the RM has been reduced from the current rate of 6% to 4%.

The Government proposes to replace the requirement that all MA eligible assets have fixed cash flows with a more flexible requirement. The Government proposes to remove the severe treatment of assets whose ratings fall below BBB and remove the clause on ring-fencing of assets. The requirement that the MA applies only to underwriting risks connected to the portfolios of longevity risk, expense risk, revision risk and mortality risk has been removed. The draft SIs state that the PRA can vary/revoke or reduce the MA benefit being claimed if a firm fails to comply with the conditions of its MA approval.

The draft SIs introduce the option for an insurer to increase the FS where necessary to ensure that it covers all the risks retained by the undertaking. The draft SIs also grant the PRA powers to disclose confidential information to publish the outcome of insurance stress testing exercises.

The Government expects that reform of the RM will be in force by year end 2023. It is also considering options to enable reforms to the MA to come into force by the end of June 2024, and the remainder of the new prudential regime will come into force by year end 2024.

See our [At a glance](#) publication for more details.

PRA consults on new Solvency UK framework

The PRA [issued](#) a consultation (CP12/23) on major reforms to Solvency II on 29 June 2023. The PRA believes its reforms will lead to a more competitive and dynamic UK insurance sector, without compromising high standards of policyholder protection. The PRA also considers the proposals will advance its new secondary objective under the Financial Services and Markets Act 2023, of international competitiveness and growth.

The PRA expects the proposals in CP12/23 to remove onerous requirements as they build on previous PRA reporting reforms and simplify the calculation process for the transitional measure on technical provisions. The PRA considers the reforms will also deliver greater flexibility, for example by replacing prescriptive PRA requirements, with a principles-based approach for assessing internal models.

The PRA states the proposals will encourage entry and increase competition through the introduction of a 'mobilisation' regime designed to allow newly authorised insurers flexibility with the PRA's requirements. For example, the proposals would allow the PRA to lower minimum capital requirements during mobilisation. Further, the proposals are expected to increase competitiveness by the removal of some requirements for branches of international insurers operating in the UK, which includes the removal of branch capital requirements and branch risk margin.

The consultation period for the PRA's substantive proposals in CP12/23 closes on 1 September 2023. Some reforms are expected to be implemented by the end of this year, and the remainder in 2024. Beyond this consultation, the PRA expects to consult in September 2023 on reforms for life insurers relating to investment flexibility and the matching adjustment. See our [Hot Topic](#) for more details.

PRA reminds general insurers to consider claims inflation risk

The PRA issued a [letter](#) to the Chief Actuaries of general insurers and Lloyd's Managing Agents on 23 June 2023, sharing feedback on its review into how firms responded to its earlier [letter](#) about the effect of claims inflation on general insurance claims. The PRA issued its letter to assist firms' preparation of their mid-year reserving exercises, and their capital and business planning for 2024.

From a sample of 16 firms, the PRA found an average claims inflation allowance in reserves of 5.9% in personal lines firms, and 3.4% across all other firms. The PRA considers these increases may not be sufficient to support future claims in relation to the forecasted economic inflation.

Therefore, the PRA is concerned there is a significant risk that the market may need to further strengthen prior years' reserves in future years and that continued high claims inflation could cause a material deterioration of the solvency coverage of some firms, unless mitigating steps are taken.

The PRA reminds firms to take proactive steps to assess the adequacy of their risk management and control frameworks given the uncertain external environment. The PRA also expects firms to reassure themselves of the continued validity of their models.

Overall, the PRA considers that 2023 year-end will be challenging for reserving teams. The PRA expects strong communication and feedback loops between functions to support reserving teams set appropriate reserve estimates.

The PRA also considers having a 'house view of inflation' may enable firms to better monitor claims inflation. Going forward, the PRA will continue to monitor and review how firms prepare for and allow for claims inflation in their reserves, claims, capital requirements and underwriting. Our [At a glance](#) publication provides further details.

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