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April 2010

EXCLUSIVE INSIGHT AND ANALYSIS FROM INSURANCETIMES, STRATEGICRISK & GLOBALREINSURANCE

Ellen Bennett ■ Executive editor

It's spring at last, and the market was in tune with the seasons this month, continuing its return to activity. In the primary space, the first major acquisitions of the year were announced – by Oval and Henderson – and other brokers continued to throw their hats in the ring for acquisitions in the months ahead. Now, it's time for less talk and more action – come on guys, we're all waiting.

And the foundations are in place: the quarterly CBI/PricewaterhouseCoopers financial services survey showed of a broker market returning to buoyancy despite continued slight drops in business volumes, with headcount up for the first time in years, and expected to continue rising.

But there was a more depressed picture for insurers. The survey found that optimism among general insurers had fallen for the first time since September 2008. It attributed the gloomy mood to a sharp decline in business volumes, income values and profitability. There's similar woe in the reinsurance market, where excess capital continues to depress rates, as seen in the Asian renewals. Reinsurers looking to grow their businesses are therefore thinking of M&A – see the deal between Max Capital and Harbor Point and expect more to follow.

Against a backdrop of political change in the UK, brokers, insurers and reinsurers alike are moving on from the financial crisis and getting ready for the next turn in the cycle. There are exciting times ahead.

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Good news and bad news

The Budget had some positive points for the industry, but how much will change after 6 May?

Most commentators were nonplussed by the recent Budget, with the general verdict that the substantial decisions on tax and spending would follow next month's general election. Nevertheless, for the insurance industry there were a couple of tasty tidbits.

Insurance premium tax

The headline news from the industry's perspective was the resolution of the row over insurance premium tax. December's pre-Budget report (PBR) sprung an unwelcome surprise on the sector by dramatically widening of the scope of IPT.

The bad news is that the scope of the tax remains wider than it was before December. The good news is that the widening is not as great as that originally envisaged when the draft proposals were published in the PBR.

Under the revised rules announced in the Budget, IPT will not be levied on fees charged by intermediaries where the level of premium has been arrived at without a comprehensive assessment of the customer's individual circumstances. Neither will the tax apply in those circumstances where the customer cannot negotiate the terms and price of the intermediary's contract.

Last week's announcement rules many brokers out of the IPT they faced having to pay under the December proposals. The changes mean that arrangement fees on personal lines like household and motors, which tend to be determined on a lump-sum basis, will generally not be liable for IPT.

And liability for any tax due under the changes will only apply from Budget day itself (24 March), not from 9 December, the date of last year's PBR. The government has confirmed that insurers, rather than intermediaries, will continue to be responsible for paying the tax.

However, while the rate of IPT stayed unchanged in the Budget, the industry should continue to be on its guard about a possible increase.

Capital gains tax

Turning to other tax matters, the rate of capital gains tax (CGT) remained the same despite considerable pre-Budget speculation that it would go up. But the big change on CGT was the doubling in the relief for the so-called 'entrepreneurs' allowance'.

The allowance covers profits on the sale of any business, including shares or assets. Under the changes, which came into force on 6 April, the first £2m of capital gains will be subject to a rate of 10%, as opposed to the general rate of 18%. If an individual were to sell a business for a gain of over £2m in 2010/11, the overall tax liability will be £380,000, representing a tax saving of £80,000 on how much they would have paid in 2009/10.

And the good news for those looking to start up a fresh business is that this allowance can be claimed over a lifetime. The additional £1m relief will also be available for vendors who have previously used this relief, but only on qualifying gains from 6 April.

The measure has been nodded through by the Conservatives, meaning that it is extremely unlikely that it will be reversed if they form the next government. However, those wishing to exit their business would be well advised to think about selling up. Even though there was no change on CGT in this Budget, an increase is widely anticipated following the general election, given the increasingly wide gap that has opened up between the new 50% top rate of income tax for earnings over £150,000 and the 18% general rate of CGT. For the insurance industry, like everybody else, the real Budget is likely to happen later this year.

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Key points

- The row over IPT seems to have been resolved in the recent Budget, with the new rules not applying in many circumstances
- The 'entrepreneurs' allowance' CGT relief has been doubled, so that the first £2m of capital gains will be subject to a reduced rate of 10%, as opposed to the standard 18%
- Despite these sweeteners, however, businesses will be watching carefully when the 'real' Budget emerges after the general election

Archive

→ Budget backtracks on IPT following industry lobbying, 1 April 2010

→ Budget 2010: No capital gains tax hike, 24 March 2010

→ Budget 2010: ABI dismay over foreign branches taxation, 24 March 2010

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Ellen Bennett • Executive Editor • Global Reinsurance

All change in Bermuda

US scrutiny on tax havens hasn't extinguished enthusiasm for the jurisdiction

All eyes are on Bermuda. The financial services market on the island is undergoing seismic change. In the absence of a market-moving event, the companies based there are making the headlines themselves.

Excess capital is continuing to dampen rates, so M&A is the name of the day – as RenaissanceRe chief executive Neil Currie joked at the recent World Insurance Forum, there seems to be an investment banker lurking behind every shopfront, looking to broker a lucrative deal.

Max Capital and Harbor Point are leading the charge, in a transaction universally agreed to look sensible on paper. It's been billed as a 'merger of equals', and will take the resulting company, to be called Alterra, past the magic $3bn mark in terms of capital.

Meanwhile, the industry grandees are clearing out to leave room for the second generation. Don Kramer has left the top job at Ariel Re in favour of long time second-in-command George Rivaz, while Ken LeStrange has handed the reins to David Cash at Endurance. The common wisdom is that their departures put their companies in play – so watch this space for news to come.

Triumph through adversity

As businesses continue to trade below book, and regulatory uncertainty in the US hovers on the horizon, deals aren't happening as fast as otherwise might be expected. However, there will almost certainly be more deals in the next six months, especially in the light of pressure from private equity investors for an exit plan.

Meanwhile, ever since US President Barack Obama publicly came out against tax havens, there have been concerns about Bermuda's viability as a jurisdiction. Flagstone Re recently became the latest company to plan a move. But companies still on the island are staunch in their defence. Despite the recent 2% rise in payroll tax, it is still an extremely business-friendly environment, and moves to elevate the financial regulator and implement Solvency II standards will improve its status.

The picture in Bermuda may be changing, but for the next few years at least, it will remain a major player on the international insurance scene.

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Key points

- Excess capital is continuing to dampen rates
- More deals will follow the merger of Max Capital and Harbor Point in Bermuda
- The domicile remains an attractive location despite US scrutiny

Archive

➔ Max Capital and Harbor Point to merge, 4 March 2010

➔ Bermuda finance minister opens World Insurance Forum, 15 March 2010

➔ Endurance chief Ken LeStrange to step down, 18 February 2010

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The race to flotation

Will 2012 be the magic year for the brokers hitting the stock market?

Flotation, flotation, flotation. That's the name of the game for some of the biggest players in insurance over the next few years.

For the consolidators, most of them backed by private equity, an exit strategy is a must. That means either a trade sale, or the much preferred route of flotation.

The main players are Towergate, Giles and Oval. All have the Olympics year of 2012 as a flotation date. At a different level, there is Hyperion – an insurance hybrid – and RBS Insurance aiming to list.

Different strategies

First, let's look at Towergate, Giles and Oval. In order to float, you need size and scale, and that's something that is proving to be problematic. As one industry insider admits, only Towergate currently has the clout to go it alone. "You need a market cap of £250m-plus," the leading executive says. "None of the other consolidators could realistically float alone – they need to get together in one form or another."

And that, indeed, has been on the cards for some time. Whether Giles buys Oval or Jelf, or whether two of the three merge, a transformational deal is a necessary prelude to the consolidators hitting the stock market.

But attitudes within the companies vary. Giles boss Chris Giles is a hawk: he has made no secret of his wish to seal a market-changing deal. Others are hanging back, though, perhaps because they are reluctant to let go of their control or their brands, or perhaps because of differing expectations regarding price.

Oval has brought in corporate adviser Rothschild to examine its float possibilities. Chief executive Philip Hodson has admitted the flotation date may be pushed back to 2015, giving the consolidator more time to accumulate premium income and perhaps enjoy the fruits of a resurgent economy.

Nonetheless, one sideshow among the consolidators will be the race to list first. Winslow says: "People like Towergate, Giles and co will be looking to get their money out by 2012, so I can see them trying to get ahead of everybody else."

Getting ready

Any company planning to list has to get its corporate house in order first. Expect shake-ups at the top, with new committees and fresh faces on board.

One company already well down that path is Hyperion, parent of broker Howden and insurers CFC and DUAL. Hyperion Group founder David Howden has already drafted in John van Kuffeler, who has 40 years' experience in both insurance and investment banking, in the role of non-executive chairman to oversee the listing process.

Howden says: "When you go to the stock market, people want to understand that the business is well run and has the right management and procedures in place."

The only company that won't need that kind of refocus for a listing is RBS Insurance, which is likely to be up for grabs by 2012, because the European competition authorities have ordered the bank to sell up. The bankers will take care of the preparations, something very much hinted by insurance chief executive Paul Geddes. "The favoured option is an IPO," he said last month, "but it may also be achieved by a trade sale. There's no hurry to do it."

The next five years are going to be interesting times in the insurance industry. Looks like the Olympics won't be the only thing to look forward to.

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Key points

- Towergate, Giles and Oval have all touted 2012 as the year they plan to float, although Oval has admitted it may push this back to 2015
- Only Towergate is seen as currently having the clout to go it alone on the stock market. Oval and Jelf will need to boost their numbers in one form or another
- Meanwhile, Hyperion and RBSI are also making preparations for their own exits

Archive

➔ Moody's lowers Towergate outlook but retains B2 rating, 8 April 2010

➔ Oval looks for mega merger, 25 March 2010

➔ Retail MD exits Giles after board revamp, 18 March 2010

➔ FSA to tighten grip on consolidators?, 17 March 2010

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The secrets of your success

Risk managers who want to reach the top of their game need to show what they're made of

With the right skills, risk managers can take advantage of the current heightened emphasis on risk management and corporate governance to propel themselves forward. During a new age of austerity there is also an opportunity, given the focus on risk and governance, if risk managers are willing to step up and take it. But what are the essential ingredients of risk management career success?

Risk managers who want to excel will need to do a number of things well. They may need to improve their business knowledge and commercial acumen, communicate better with the board, as well as overcome some tricky political problems that they will inevitably face, acting as they do as the conscience of the business.

Improve business knowledge and commercial acumen

The most important thing for risk managers is to be seen as business-enabling, not as an obstacle to doing business. Judging by the experience of some in the financial sector of late, it is easy for troublemaking risk managers to be brushed aside.

In order to be seen as business-enabling, risk managers need to talk the same language as the business, which could mean doing some financial training. They must also integrate themselves into the business rather than being tacked onto projects at the last minute.

If risk managers want to become more involved, they need to put forward solutions not just problems. In their presentations to the board, it is no good simply bringing risks to the board's attention and abdicating responsibility for managing them. A good approach is to present the risks while at the same time offering guidance on how to deal with those issues, either in the form of recommendations or – better still – innovative solutions.

Communicate effectively with the board

Communicating with the board needs to be done quickly and succinctly. It is no good getting bogged down in the intricacies of an insurance contract. The board's time is precious, so if risk managers have the opportunity to speak to them, it is imperative that they use that time wisely. It may be that a risk manager is called on to deliver a report to the board during a crisis. Moments like these can be career defining. The risk managers who succeed will be the ones able to demonstrate the skills they have and the value that they bring to the role.

Tackle complex political issues

Clearly, it is important not to be too adversarial. However, a time will arise for most risk managers where they have an opinion that is directly at odds with other parts of the business. An example is a business unit that is looking to steam ahead with a new product line, but the risk manager is much more cautious because of huge risks associated with the undertaking. Risk managers faced with similar circumstances should not feel alone. Sometimes they may feel compelled to bypass executive management and go directly to the non-executives with their concerns. This is a huge problem, but it is one that can be overcome.

The advice is to be measured. Try not to compete with the business development department. Rather, present a balanced case with the right level of research and analysis, using data to support the argument. Make sure that senior management are aware of the potential risks as well as the rewards. It may be that, in the end, the risk manager is still over-ruled, but it is better that they have put their view across and it has been documented. Whether or not the business is willing to listen to the voice of caution depends on the culture and the tone from the top.

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Key points

- Risk managers should be business-enabling not an obstacle to bypass
- They need to integrate themselves into the business and speak the same language as senior managers
- Presentations to the board should be succinct and include solutions, not just problems
- Conflicts will arise, but these can be managed by treating the business with respect

Archive

→ Risk managers exonerated, 6 April 2010

→ Airmic podcast gives career advice, 30 March 2010

→ Test your risk intelligence, 18 January 2010

→ Survey says ERM moves on, slowly, 12 January 2010

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