

The Impact of the EU Referendum

Welcome to Willis Tower Watson
Nicolas Aubert, Head of Great Britain.

Agenda

Time	Subject	Speaker
09:00 – 09:15	Welcome and Introduction	Nicolas Aubert, Head of Great Britain, Willis Towers Watson
09:15 – 09:55	Brexit: Potential Scenarios & Corporate Planning	James Middleton, UK Head of Legal AIG
09:55 – 10:25	The Potential Impact on Regulation and Risk Management	Darren Holmes, Head of GB Risk Management, Willis Towers Watson
10:25 – 10:55	COFFEE BREAK	
10:55 – 11:25	The Implications for Investment	Robert Hayes Brown, Chair, Global Investment Committee, Willis Towers Watson
11:25 – 11:55	The Potential Impact on Pensions	Mark Dowsey, Senior Consultant, Willis Towers Watson
11:55 – 12:25	Engagement, Talent and Reward implications	Rich Veal, Head of GB Talent and Reward, Willis Towers Watson
12:25 – 12:35	Closing	Ailsa King, GB Head of Clients, Willis Towers Watson
12:35 – 13:30	LUNCH	



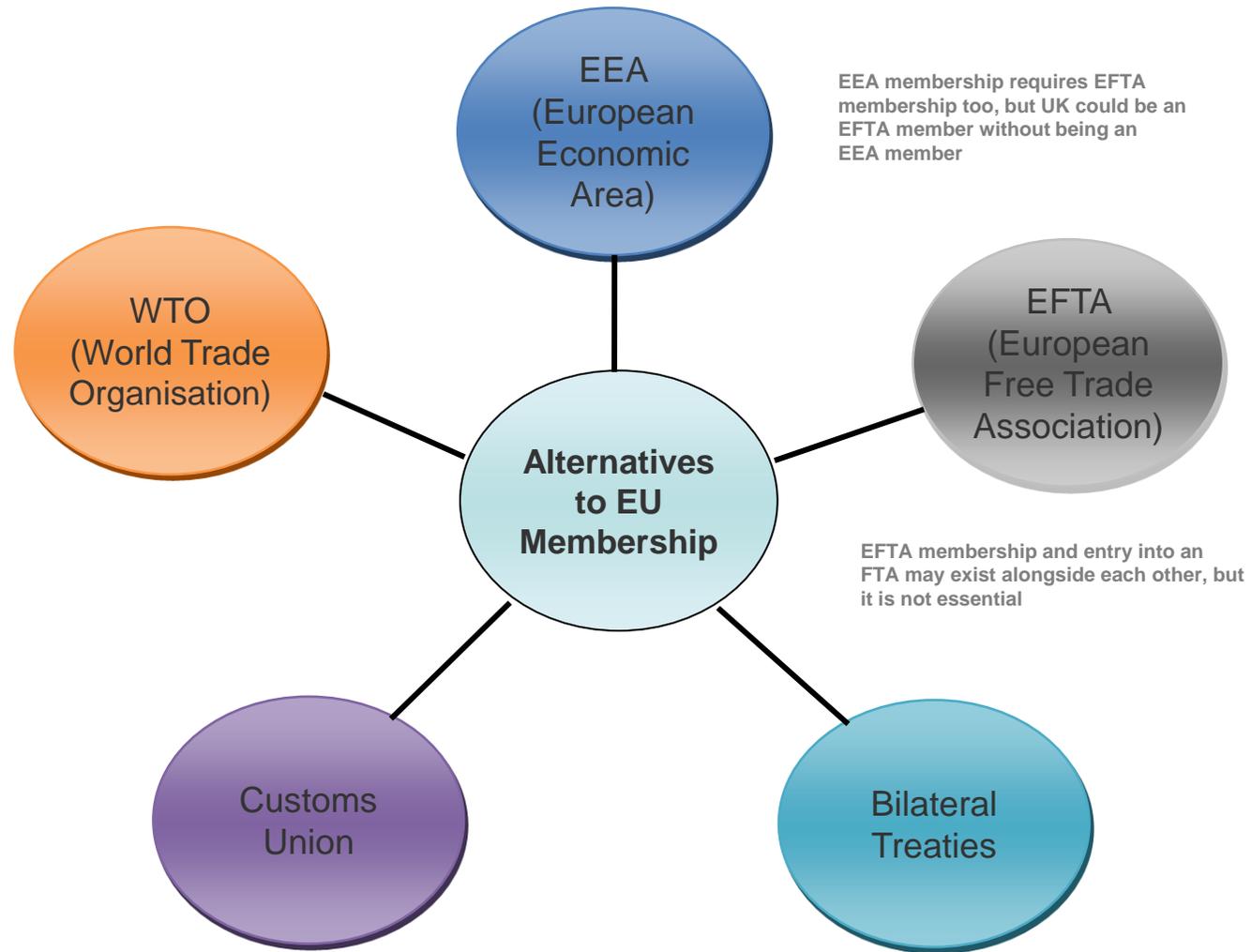
Brexit: Potential scenarios & Insurance

29 June 2016



Brexit scenarios

Potential EU Alternatives



EEA + EFTA membership



"The Norway Option":

- UK would leave the EU and emulate Norway in becoming a member of the European Economic Area and the European Free Trade Association.
- All 4 current EFTA members would have to consent – would they agree to retain UK opt-outs?
- Obligated to implement the vast majority (Norway estimates 75%) of EU legislation (main exceptions being energy, fisheries and farming), but no voice at the negotiating table.
- Subject to jurisprudence of EFTA court – incorporation into UK law
- Reimposition of UK tariff and trade regime (outside of Customs Union)
- For Financial Services, maintains passporting
- Freedom to conclude trade agreements with third countries (no longer part of Customs Union and Common Commercial Policy) – but would they be more favourable?
- In Cameron's January 2013 Bloomberg speech on the EU, he openly set out a position against Britain being in the EEA but not the EU.

Bilateral Treaties + EFTA



“The Swiss Option”:

- The UK would leave the EU but agree sector-by-sector treaties with the EU, and free trade agreements with the EFTA countries.
- There are currently over 120 bilateral agreements in force between Switzerland and the EU: not clear that the EU has appetite to repeat this model - 9 years to put in place.
- Enforcement of the agreements within Switzerland is solely in Swiss hands - there is no agreed enforcement mechanism
- .
- Bilateral agreements not automatically updated with changes to EU legislation – divergence until re-synchronised: creates cost for business.
- No access to Internal Market for Financial Services (other than branches of non-life insurers).
- Not a comprehensive solution

Customs Union



"The Turkey Option":

- The UK would leave the EU and enter into a Customs Union with it.
- Access to the EU Internal Market for goods without the need to comply with EU Rules of Origin for non-EU countries and significant portions of the EU Common Commercial Policy, state aid and competition rules. Otherwise, no obligation to impose EU laws.
- UK would have to impose the EU common external tariff on imports from outside the UK/EU customs union
- UK would have to abide by EU regulations in relation to goods, i.e. product standards
- UK would lose its current right to provide services on equal terms with EU members (reliance on GATS).
- This option is considered to work reasonably well for goods, but not so for services. As a net exporter of services, it is not likely that this option would be pursued by the UK.

World Trade Organisation



- Purest form of “out” ...maximum sovereignty?
- Potential loss of benefits of some 50 EU Free Trade Agreements with third countries
- Limited “clout” and resource
- UK would be subject to the EU common external tariff on trade with the EU
- UK would have to abide by EU regulations in relation to goods, i.e. product standards
- Recognition of “right to regulate” - EU has “prudential carve-out” under the GATS Annex on Financial Services – allows it to take prudential regulatory measures are deemed necessary to intervene in trade in financial services between the UK and the EU so as to protect investors, depositors, policyholders, etc. – potential loss of current advantages.



Insurance Industry Impacts

Insurance sector impacts

Financial Services Regs	Data Protection	Insurance Policies
<ul style="list-style-type: none"> Impact on “Passporting”: <ul style="list-style-type: none"> Freedom of Establishment Freedom of Services Solvency II – will the UK apply for, and be granted, equivalence? Ability to hold single capital pool under single prudential regulator for pan-European UK insurers and EEA insurers with a UK branch. 	<ul style="list-style-type: none"> Existing EU data protection law prohibits transfer of personal data outside the EEA unless one of a prescribed set of conditions is met. UK becomes non-EEA destination: <ul style="list-style-type: none"> - Would EU grant equivalence? - EU-US Privacy Shield model? - Standard Contractual Clauses 2018 – new General Data Protection Regulation Will UK implement? 	<ul style="list-style-type: none"> Abandon EU more “purposive” approach to interpretation? Busy courts – slower claims? D&O / PI claims for failure to properly prepare / advise? Some wordings may need more updating than others e.g. environmental / product liability rules largely derive from EU law.
Customer Conduct	Reinsurance	London as a hub
<ul style="list-style-type: none"> Consumer protection legislation (whether or not it derives from EU rules) largely embedded in UK law. No dramatic changes expected. Consumer rights derived directly from EU Regulations in theory fall away: <ul style="list-style-type: none"> scramble to replicate in UK law then amend over time? pick and choose clause by clause what UK writes into own law? 	<ul style="list-style-type: none"> Absent another agreement, any EEA states may deny local cedants credit for the reinsurance unless UK reinsurers post collateral in their favour. Adds cost? – including to captive arrangements 	<ul style="list-style-type: none"> London is the world’s largest insurance market. The UK now offers the best of all worlds - access to both the London market and the single market. A key part of an emerging market insurer’s diversification strategy is through London and Lloyd’s: greater competition from other insurance centres around the world?



Corporate Planning

Public Affairs

- Lobbying?
- Industry bodies

Communications

Clients
Industry
Staff

Risk

- Impact of uncertainty
- Operational Risk
- Market Risk

Regulatory

- Keeping regulators informed
- Would different rules EU vs UK add cost?

Corporate Planning

Sales

- Tariff impact?
 - Grow differently?
- Impacts long term growth plans?

Legal impact

- Contract certainty
- Massive legislative change
- Busy courts

HR

- Impact of loss of freedom of movement
- Staffing levels impacted?

Corporate Governance

Involvement of Board / Committees



An aerial photograph of a city street grid, showing buildings, roads, and green spaces. Several white rectangular redaction boxes are placed over the image, obscuring parts of the street layout and buildings. The boxes are located in the top right, middle right, middle left, bottom left, and bottom right areas.

The Potential Impact on Regulation and Risk Management

Darren Holmes – Head of GB Risk Management

Introduction

Background to our Regulatory Framework

- 1973 - Joined the EU
- 1974 - The introduction of the “Health and Safety at Work Act” UK Based Legislation
- 1989 – Introduction of the European Health and Safety Framework Directive
- 1997 to 2009 – 41 of 65 new regulations originated from the EU
- 2010 to 2016 – reduction in pace of new regulation due to EU commission taking a less regulatory approach

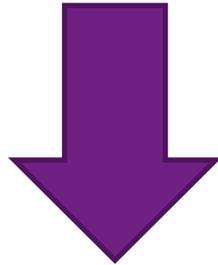
The Impact

The suggested impact of the EU on Safety

1989 = 368 Fatalities in the UK

2015 = 142 Fatalities

Between 2005 and 2015 – number of fatalities have plateaued



coincides with the reduction in legislation from the EU and decline in enforcement activity in the UK caused in part by the reduction in government funding of regulatory enforcement bodies

Legislation Changes

The Focus

EU Directives require that the requirements are written into UK Law such as:

- H&S
- Chemicals
- Working time

EU Regulations are not written into UK Law and as such will need to be written and may result in changes to current legal requirements, These include (but not limited to):

- Food,
- Cosmetics
- Data Protection/Privacy
- Some area of product liability
- Trading standards
- Environmental

What does the Future Look Like

- All current views on the impact on regulation when we exit from the EU point to the same answer – “Unknown”
- Proposals already made by the UK to the EU to reduce regulation and being out may see this reduce further
- Less regulation on SME and self employed
- More revenue generated by the introduction of the Sentencing Council Guidelines on H&S Food Safety and Corporate Manslaughter
- Focus on Self Regulation with the introduction of the Better Regulation Delivery Office (BRDO)
- A view is held by some that the momentum for “Health” in the workplace may loose focus as we have less access to data and analysis from the EU

The Immediate future

Next 2 years

- Bound by a 2 year notice period where EU directives will remain in force
- No change in the short term due to the time required to consider new regulation
- Focus on maintaining trade opportunities with Europe
- Ensuring risk management processes are effective to ensure consistent approach across EU and Non EU countries – individual regulatory requirements

Longer Term View

- Membership with the European Trade Organisation (EFTA) requires compliance with a number of Social and Employment laws imposed by the EFTA
- Trading internationally has evolved and more focus on ethical trading requires demonstration that systems are in place
- Greater focus on the supply chain and the impact of trading partners on brand and reputation
- Creating our own laws and maintaining enforcement will no doubt see our enforcing bodies evolve
- Regulatory compliance is only one aspect of a corporate risk register –ensure your approach is fluid enough to adapt to the uncertainty of change

Summary

Priorities

Short Term

- Risk leadership and clarity of message
- Review your risk management approach to ensure it is suitable to respond to immediate changes and volatility
- Consider your appetite for risk and does this need reviewing in light of uncertainty
- Increase the pace in which your risk register is reviewed and monitored

Medium Term

- Engage with your stakeholders in the supply chain and work collaboratively together to mitigate risk
- Be consistent in your messaging on risk and opportunity and keep people informed

Long Term

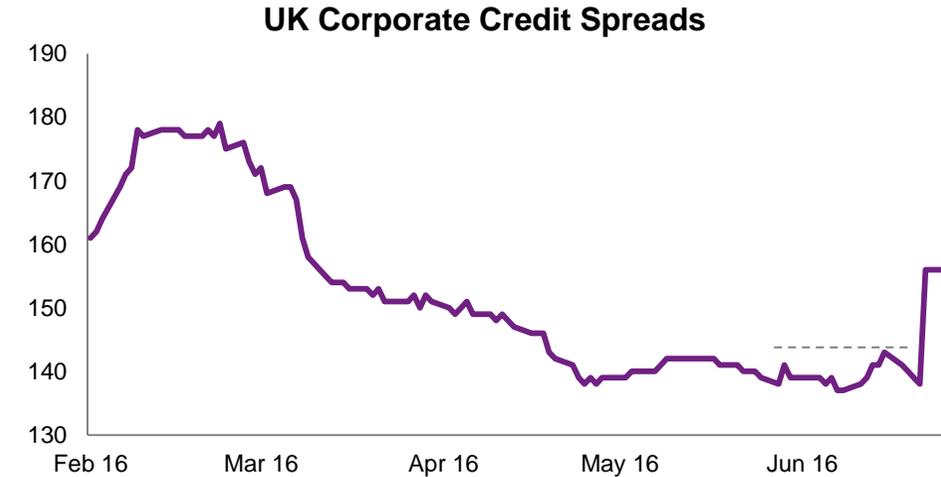
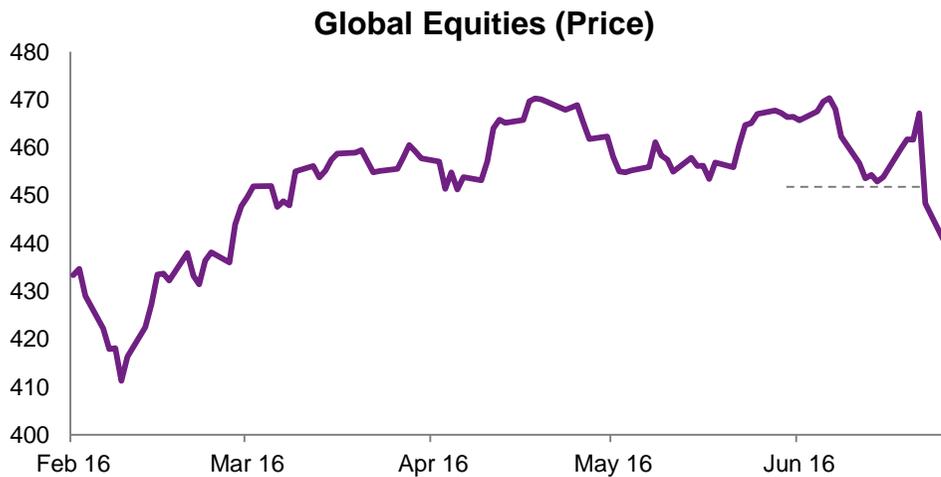
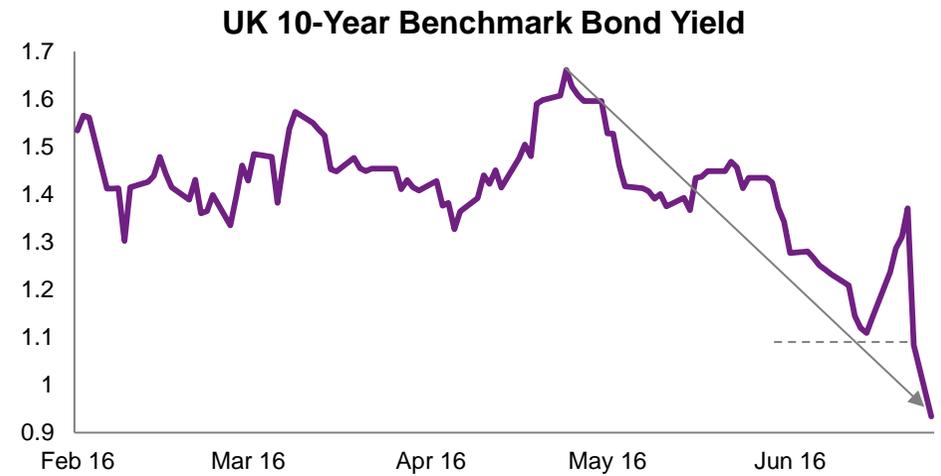
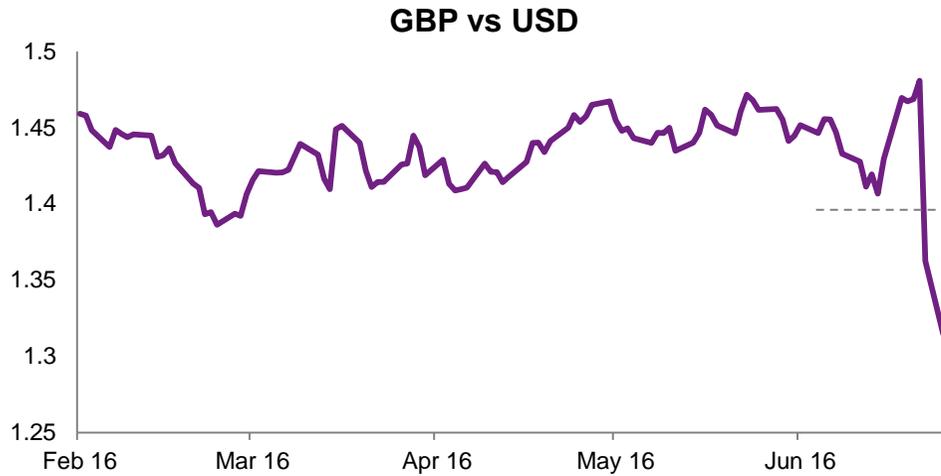
- Encourage people to think about how the future may impact your organisation
- There are both risks and opportunities which may emanate from the changing landscape - think ahead.

The Implications for Investment

Robert Haynes Brown
Chair, Global Investment Committee
Willis Towers Watson

Market moves

Market action in response to the “leave” vote

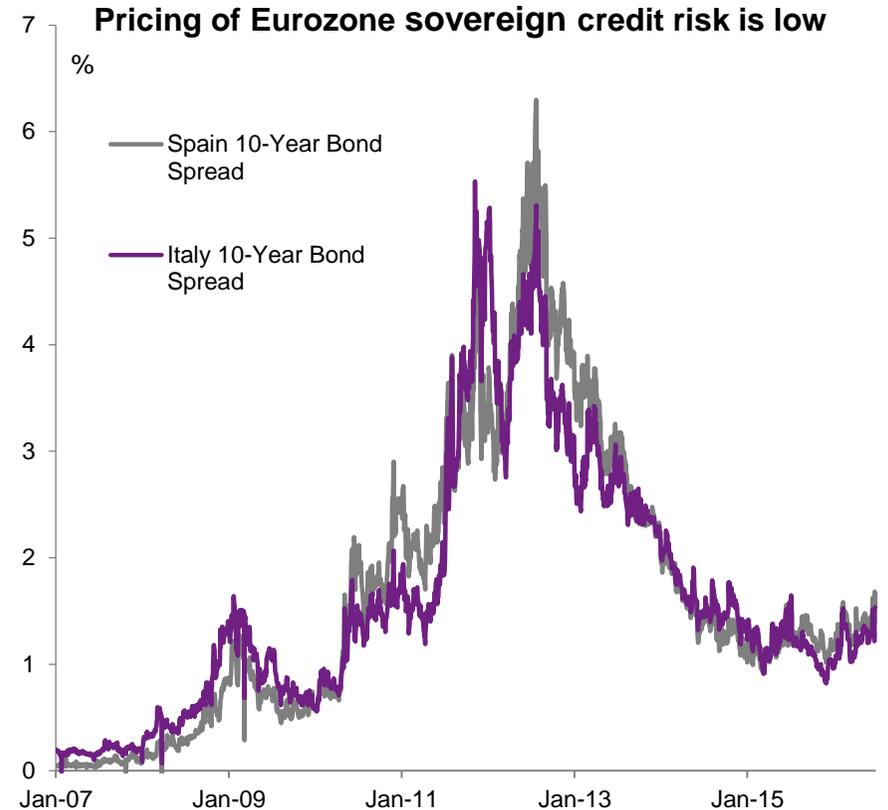


Source: Factset

Political events

The risk to the Eurozone project and constraints on EU policy

Country	Things to watch
U.K.	<ul style="list-style-type: none"> • New Conservative party administration • “Highly likely” to be new Scottish independence referendum
Eurozone	
Spain	<ul style="list-style-type: none"> • Elections - 26 June 2016 • Possible momentum for Catalonia independence
Italy	<ul style="list-style-type: none"> • Referendum on Renzi’s constitutional and economic reforms - October 2016
France	<ul style="list-style-type: none"> • Presidential election in April and May 2017
Germany	<ul style="list-style-type: none"> • Federal election in September and October 2017
U.S.	<ul style="list-style-type: none"> • Presidential election in November 2016



Source: Factset, WillisTowersWatson

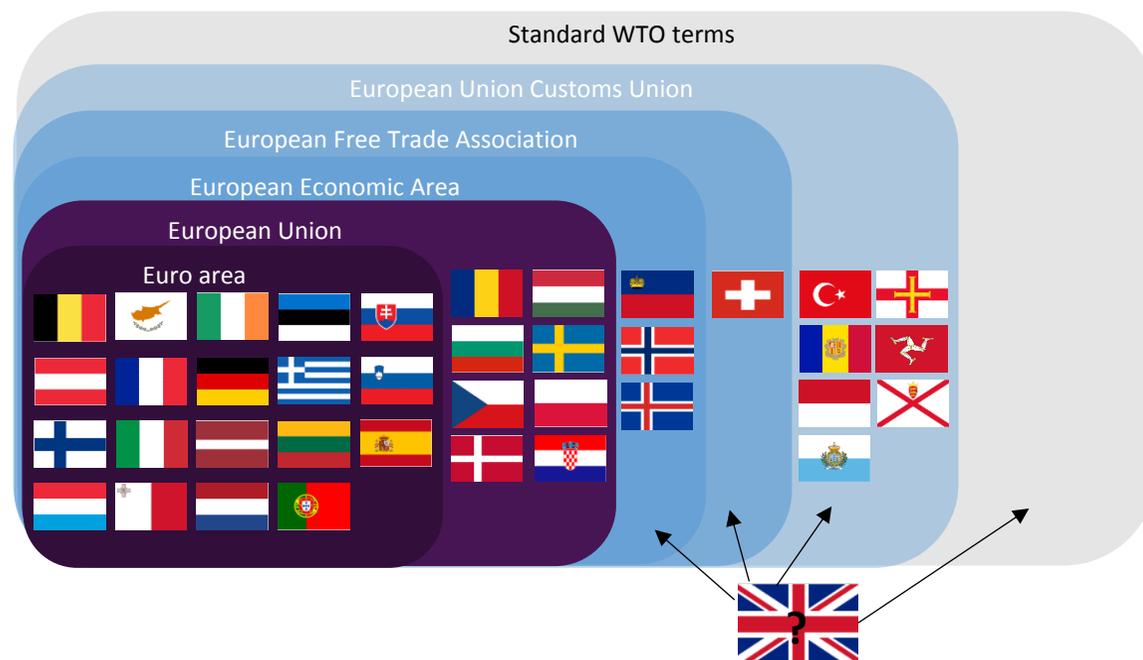
UK economy and policy

Growth & inflation

- Lower productivity already occurring
- No initial change to way goods/services/people move
- Slowing investment from uncertainty
- Long-term economic impact depends on trade agreements
- Higher inflation short-term from GBP weakness

Bank of England policy

- £250bn of liquidity to stabilise financial system
- Possible credit easing in July
- Possible rate cut in August



Source: LGIM, WillisTowersWatson

Capital markets

Things to watch

Asset Class	Key drivers of 24 th June market action	Key drivers of medium-term outcomes
Sterling	<ul style="list-style-type: none"> • Short-term capital flows to “safe haven” currencies, e.g., Swiss franc, yen • Uncertainty over future UK terms of trade • Lower foreign investor confidence and expectations for weaker domestic conditions 	<ul style="list-style-type: none"> • UK current account deficit a pressure for weaker sterling • Terms of trade uncertainty and weakening domestic conditions also moderately negative for sterling • Easier Bank of England policy is moderate downward pressure on sterling
Short & long rates	<ul style="list-style-type: none"> • Short-term investor asset allocation shift to “safe-haven” asset classes • Gilt yields fall on expectations of easier future Bank of England monetary policy 	<ul style="list-style-type: none"> • Bank of England likely to engage in credit easing and interest rate cut to support weaker domestic economy • Declines in short-term and long-term government bond yields broadly warranted under such policy
UK Credit & Equity	<ul style="list-style-type: none"> • Lower prices due to higher risk premia required by investors 	<ul style="list-style-type: none"> • Whether cash flow generation is above or below market expectations – linked to UK and European economic conditions and policy • Extent to which central banks ease financial conditions, which reduces risky asset discount rates

Source: WillisTowersWatson

Investor implications

Three key messages in the face of uncertainty

- 1. Strategy:** Recent market action comes on top of already material declines in yields so far this year – an important catalyst to take a hard look at strategy; consider return assumptions that project asset returns to stay “lower for longer”
- 2. Currency Risk:** UK schemes will see big short-term currency hedging outflows that will have to be met from liquid assets – a close eye on schemes leverage, liquidity and currency hedging positions is warranted
- 3. Stress Testing:** Utilise stress testing frameworks to manage risk and opportunity as the politics, economy, policy and market pricing evolve

The Potential Impact on Pensions

Mark Dowsey – Pensions Technical Unit
Senior Consultant
Willis Towers Watson

BREXIT

Overview		23 June – vote was to leave; but not what happens next
Treaty (Article 50)		<ul style="list-style-type: none"> • Member State notifies Council • Negotiate terms of withdrawal Agreement between UK and Council subject to consent of European Parliament • Council conclusion subject to SQM ($\geq 72\%$ countries and $\geq 65\%$ population)
Timing?		<ul style="list-style-type: none"> • Two years from notification – unless unanimous agreement to postpone
Options (broadly)		<ul style="list-style-type: none"> • Renegotiated deal with EU – back in ‘reformed’ EU • Norway or Swiss model (£115pc/£53pc²⁰⁰⁹) • Free Trade Agreement
Treaty Freedoms		<ul style="list-style-type: none"> • <i>Art 26</i> – states that "the internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured..."
Cost?		<ul style="list-style-type: none"> • £X million per week saved.....(£152 pc)

Brexit – the potential impact on pensions in the UK

Overview

Although there is little EU legislation that **directly** relates to UK pensions, the IORP (Pensions) Directive and various EU employment legislation do have an impact on UK pensions.

Other ‘indirect’ effects will be felt – including through markets

IORP Directive

- the Scheme Specific Funding Requirement
 - Cessation of ‘death benefit’ only OPSs
 - Cross-border rules
 - SIP/report and accounts, in accordance with extant UK requirements
-

Insolvency Directive

- PPF
 - Concerns CJEU could increase compensation level
-

Anti-discrimination

- Age, sexual orientation and disability
 - Sex discrimination – including agency, part-time and temporary workers
 - Equalising for effect of GMPs
 - Parental leave
-

Brexit – the potential impact on pensions in the UK

Acquired rights on transfer

- TUPE (Transfer of Undertakings Protection of Employment) regulations (and 'TUPE-style' provisions in 2004 Act)

Data protection

- General Data Protection Regulation

What about the effect of wider factors?

- Investment volatility
- Impact of financial conditions for 30 June reporting date
- Effect on sponsor covenant
- Effect on financial service providers – contract-based arrangements (potential loss of passporting rights)
- Scottish independence

Can we expect a 'red-tape' bonfire?

- 1997 -2009 6.8% primary legislation and 14.1% secondary
- 2013 'red tape challenge' results – amalgamation of OPS and PP Disclosure Regs and removal of statutory requirement for the maintenance of a trustee register
- Divergence with EU – no 'IORP II', no 'HBS' (or Common Framework BS) and no risk of another 'Test Achats'-style judgment

Brexit – actions to take

Covenant

- Re-assess in light of effect of Brexit on sponsor business plans

Funding

- Call early valuation to reassess funding assumptions and any recovery plan?

30 June reporting

- Ensure sponsors have a handle on how financial conditions have affected their employee benefit liabilities
- Ensure monitoring in place to avoid MI shock

EU-based sponsor

- Consider PPF eligibility
- Consider effects on any guarantee given

If detriment expected

Consider what can be done to mitigate costs – close to DB accrual, review DC with view to cost cutting

Investment and other issues

Review interest rate/inflation hedges
Consider impact on option pricing
Monitor hedge/option triggers
Effect on buy out costs

Engagement, Talent and Reward implications

Rich Veal

Head of GB Talent and Reward

Willis Towers Watson

Don't panic

Emotions first

Values matter

Keep people engaged

Actively listen

Resilience second

Change ready

Segmentation

Staying on track

Implications third

Volatility

Performance

Talent

Don't panic

1. **Emotions** – help employees progress to the new normal
2. **Resilience** – you can prepare for the unknown
3. **Implications** – keep your reactions in proportion and in context

Closing

Ailsa King

GB Head of Clients

Willis Towers Watson

In Summary...

Insurance

Consider long term growth plans
Keep regulators informed

Risk

Review approach and ensure it works in the 'now' environment

Investment

Volatility will continue. Need to stress test strategies and investment and currency risks

Pensions

Ensure your sponsors have a handle on how financial conditions have affected their employee benefit liabilities
Consider what can be done to mitigate costs

People

Keep calm. Recognise emotional impact on your people. Address that through change and engagement programmes. Essential to keep focus on BAU

**We have deep expertise in all these areas and will work with you through this period.
Contact any of us – even just for a chat.**