

A photograph of a city skyline at night, featuring several tall, modern skyscrapers with illuminated windows. In the foreground, there are silhouettes of people walking on a set of stairs. The image is partially overlaid with decorative geometric shapes: a red rectangle with white concentric circles on the left, and a purple rectangle with white concentric circles on the right.

Global FINEX - Financial Institutions UK Asset Management market update

H1 – 2022

Executive summary

We entered 2022 with the hope the lingering effects of the COVID-19 pandemic were hopefully fading and that life for many was beginning to resemble something close to normal, but the Russia / Ukraine conflict brought yet another major challenge for the world to contend with. Despite the volatility of the first two years of the decade, the asset management industry has, by and large, proved resilient to dealing with macro-economic shocks, the rising tide of regulation, and increased scrutiny from investors. The sector has, of course, also had to deal with the ever-evolving demands of the insurance industry.

In this UK Asset Management Insurance Market Update (as of 31st March 2022), I am pleased to provide FINEX UK's thoughts on the current state of the UK insurance market for non-publicly traded asset managers and the funds they manage. This update also gives an insight into what to expect for the rest of 2022, and where we are in the insurance market cycle. We also provide updates on some of the issues highlighted in the last [update](#) and identify emerging issues, in addition to discussing the likely impact on investment management insurance policies.

We acknowledge the last few years of procuring Professional Indemnity (PI), Crime, and Directors' and Officers' (D&O) Liability insurance – collectively known as investment management insurance (IMI) – has been a challenge for a large number of asset managers. This was largely down to the insurance industry being on a poor financial footing as the result of the longest 'soft market' ever known after the natural catastrophe losses of 2017 filtered through the insurance market. The result was premiums had to rise slightly, which they did generally in 2018/19, in order to support the sustainability of the UK insurance market. COVID-19, however, added fuel to the fire and insurance capital fled, leading to one of the hardest markets in living memory. While this has proved difficult, the good news is hard markets have been short-lived historically, and there are promising signs the current hard market will follow suit.

Much has been written by both insurers and brokers about where market rates are heading. It will come as a relief for most asset managers to know premiums are stabilising. The combination of aggressive insurer growth targets and an injection of new capital has meant that, to an extent, healthy market forces have returned. It should be noted that while this is the case for IMI, this does not apply to every insurance class, including cyber. Overall, it would still be prudent to budget some increase as insurers will factor material changes to a firm's risk profile, such as growth in revenue/assets under management (AUM), opening of overseas offices, changes to regulatory supervision and claims, to name a few, when providing renewals terms. It should also be noted that although insurance market conditions have much improved, it would be misleading to say premiums are currently flat or falling across the board as some may suggest. However, at WTW, we remain focused on working to negotiate better terms from insurers on behalf of our clients, and manage clients' expectations accordingly by building honest and constructive relationships to support better outcomes.

Environmental, social, and governance (ESG) remains high on the agenda of firms and regulators worldwide, with increasing engagement at board and senior executive level on a range of issues. Notably, COP26 brought climate change into sharp focus. Other current areas of focus are the government's post-Brexit review of the regulatory framework for financial services and the operational resilience of firms, including the challenges brought by recent geopolitical events in Eastern Europe. Against this backdrop, firms proactively engaging with their brokers will be more likely to succeed in obtaining more favourable insurance terms.

Should you have any questions or wish to discuss any of these issues in greater detail, please do contact me or a member of your WTW team.

Henry Keville
G.B Head of Financial Institutions
Henry.Keville@WillisTowersWatson.com

PI, Crime and D&O (IMI) market update:



Premium and retentions

Primary premiums: Budget for a further 0-5% increase on 2021's renewal for asset managers whose risk profile remains broadly the same.

Excess premiums: Mostly following the increases as set by the primary insurers but with increased competition amongst insurers, a flat renewal is achievable.

Retentions: Largely remaining flat.

Exceptions: Asset managers with challenged risk profiles and/or significant claims activity are likely to see continued upward pressure to both premiums and retentions.



Markets

- **Cracks are appearing:** During the last few years, insurers were uniform in their approach of holding firm on imposing premium increases, with very few willing to undercut their competitors, despite a handful of new entrants. So far in 2022, the impact of a number of insurers having aggressive growth targets coupled with the prospect of facing new insurer entrants also looking to grow their market share, is seeing insurers adapting to these challenges.
- **Increased flexibility:** Due to the above, we expect incumbent insurers on programmes to be more flexible with their renewal terms if challenged by competing insurers. On the flip side, we expect insurers to compete more aggressively for new business. In short, allow WTW as much time as possible to canvass the market with a view to negotiating better terms.
- **Relationship considerations:** Caution should be taken when looking to replace long-term primary and/or excess insurer partners with new insurer entrance.



Targeted segments

- **Insurer appetite:** The asset management sector is still an area the majority of insurers want to grow.
- **Private equity and real estate:** Still the most challenged and least desired sectors by insurers currently, due to the impact of COVID-19 on their investment portfolios. However, insurer appetite is slowly changing with insurers sure to target these sectors more aggressively later in 2022.



Capacity

On the up: Insurers are no longer looking to reduce the amount of capacity they deploy for renewals. If anything, insurers are now looking to increase the amount of capacity they deploy for certain clients, the idea being this is a good way for insurers to achieve their growth targets. We expect this trend to accelerate as 2022 progresses.

New entrants: We expect new insurer entrants to really start challenging and creating more of a presence on programmes.



Coverage

Non-cyber-related coverage: Broad IMI coverage is largely available with most insurers not looking to reduce traditional coverages as may have been the case during the last few years.

Cyber: Financial Institution underwriters have recently been trying to eliminate ambiguity for cyber-related claims under IMI insurance policies by adding language, such as 'silent cyber' endorsement, clarifying what is, and what is not, covered. However, some insurers have gone a step further by explicitly removing cyber extortion/ransomware coverage from the crime section of IMI policies. This has meant a number of asset managers have faced the challenges of obtaining a standalone cyber policy which, given the current insurance market conditions for cyber, is not a straightforward task. We elaborate further on this under the '[Key issues to watch](#)' section later in this document.

Continued impact of the COVID-19 pandemic

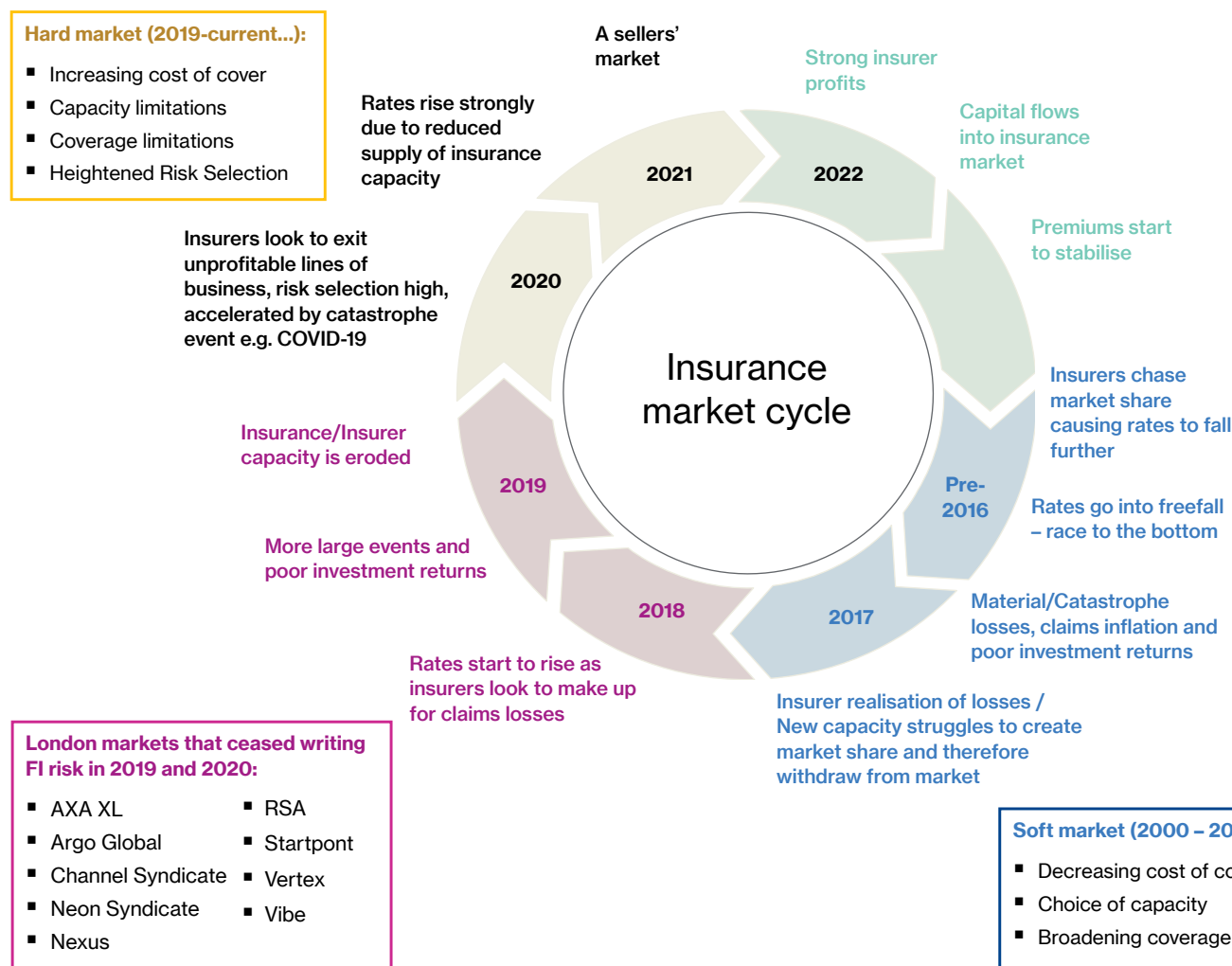
- Insurers are still carefully reviewing the risk profiles of asset managers, including the composition and performance of investment portfolios.
- We expect extensive questions on plans for returning employees to the workplace and the impact of hybrid working on investments.

Continue to allow sufficient time during the renewal process.

Current insurance market cycle 'radar'

Putting things into perspective for 2022

- Premium increases are levelling off and if there is market appetite, flat renewals are very achievable.
- Insurers will still look to increase premiums for clients whose risk profile has increased down to factors such as substantial growth, opening offices in North America and the like, or having suffered claims.
- We expect new insurers that have entered the market over the last 12 months or so to start aggressively competing for market share.



Key issues to watch

COVID-19: Back to work challenges



Observation:

Whilst new Coronavirus variants are still likely to emerge, largely thanks to governments looking to lift restrictions, many employers are grappling with implementing their new ways of working. This could involve asking some staff to return to the office full time, others part time and some to work purely from home.



Concern:

Numerous issues can arise when trying to distinguish between different roles and trying to communicate a firm's 'return to the office' strategy. It could be the difference between retaining staff and, indeed, attracting new talent. There is also the potential for discriminatory related claims to arise.



Suggestion:

Discriminatory related claims involving members of staff would usually fall either under an IMI policy or a separate standalone Employment Practices Liability (EPL) insurance policy. Care should be taken to understand the breadth of cover afforded under such policies as to whether discriminatory claims against an insured person and/or insured entity are covered. We expect questions from insurers around your 'return to the office' strategy when renewing either of the above insurances.

Market volatility



Observation:

With the COVID-19 pandemic and its initial impact on global markets now behind us, all eyes are set on the effect of rising inflation, rising interest rates, the escalation of the crisis in Ukraine and the resulting geopolitical tensions it is causing. Market volatility is here to stay for a while longer.



Concern:

Historically, periods of extreme market volatility result in greater claims activity, usually beginning with errors made during the associated spike in trading activity, followed by litigation brought by unhappy investors (often by alleging a breach of mandate) and potentially, regulatory activity against the adviser and/or funds.



Suggestion:

Asset managers should ensure their trade error manuals require immediate notification of such errors to the internal contact responsible for insurance who can in turn inform their insurers via their brokers within the necessary time frames. Failure to do so could lead to insurers denying the coverage.



Key issues to watch

continued

Alternative Investment Fund Managers Directive (AIFMD) II



Observation:

The European Commission on 25th November 2021¹ issued its proposals to amend existing AIFMD rules. This includes changes to the following:

- Changes to delegation arrangements for authorised Alternative Investment Fund Managers (AIFMs)
- Delegation arrangements for authorised AIFMs
- National Private Placement Regime (NPPR) framework
- New substance requirements for EU AIFMs.



Concern:

Although we do not expect any of the above proposed amendments to enact before 2024, considering the EU's legislative process, alternative investment managers across Europe (especially in the UK in light of Brexit) and the rest of the world, will no doubt be following developments with interest.

Asset managers are often built on delegating services to different parties, therefore we expect the EU to challenge the status quo of AIFMs delegating mandates to advisers outside of the EU to the UK. Much focus will continue to be on the UK and EU agreeing a memorandum of understanding on a framework of regulatory co-operation for financial services.



Suggestion:

Much is uncertain as we wait to see how AIFMD II materialises but in the meantime, ensure your insurers are licensed in the EU should events during the policy period make it necessary to set up entities for which insurance is sought.

1. https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12648-Financial-services-review-of-EU-rules-on-alternative-investment-fund-managers_en

Key issues to watch

continued

Financial Conduct Authority (FCA)



Observation:

With the **Financial Services Act 2021** now being law, the FCA has continued its ambitious transformation programme, putting consumer protection at the heart of its focus on becoming a 'more assertive, innovative, and adaptable'² regulator. Leading the charge, the introduction of a new Consumer Duty is expected to bring about a step change in how financial sector firms behave. From 1st January 2022 the UK's Investment Firm Prudential Regime (IFPR), represents a significant overhaul of the current rules, both in terms of the way investment firms are categorised from a prudential perspective and in terms of the requirements to which they are subject. Essentially IFPR aims to simplify the requirements for firms regulated in the UK under the Markets in Financial Instruments Directive (MiFID). The final rules can be found in **FCA 2021/38** and **FCA 2021/39**. Key points to note include the increased regulatory capital requirements, new reporting and remuneration rules, and increased disclosure requirements. Other developments for 2022 include proposals to improve regulated firms' oversight of Appointed Representatives.



Concern:

Solo-regulated MiFID investment firms as well as AIFMs or Undertakings for Collective Investment in Transferable Securities (UCITS) management should assess the likely scope and consequences of the new regime. More than ever, increased regulatory scrutiny for asset managers increases the chance of a regulatory investigation. At a time when the insurance market is still in a challenged state, this could lead to insurers reducing the scope of investigations cover and/or significantly increasing the costs for such cover.



Suggestion:

Asset managers should refresh their understanding of the scope of regulatory investigations coverage afforded under their IMI policy, paying particular attention to how such cover is triggered and whether the entities and/or individuals are covered.

2. <https://www.fca.org.uk/news/press-releases/fca-commits-being-more-innovative-assertive-adaptive-regulator>



Key issues to watch

continued

ESG



Observation:

ESG remains and will continue to be an area of regulatory focus for 2022. At the beginning of the year, the FCA introduced a requirement for UK regulated asset managers to disclose how they take climate-related risks and opportunities into account in managing investments. Similar to the Sustainable Finance Disclosure Regulation (SFDR) which requires managers of Alternative Investment Funds being marketed in Europe, it requires asset managers to make disclosures about the climate-related attributes of their products. Both the Prudential Regulatory Authority (PRA) and the FCA, have both made it clear it is not just about the 'E' of ESG that is of importance here, but that they are committed to 'accelerating the pace of meaningful change' in diversity and inclusion in the financial services sector as well.



Concern:

Asset managers subject to SFDR must ensure they keep on top of the implementation timeframes and introduce the necessary protocols ahead of 1st July 2022 (required in relation to Article 8 or Article 9 products) whilst also keeping an eye on any differing requirements being proposed by other regulators such as the FCA or Securities Exchange Commission (SEC).



Suggestion:

We expect insurers to inquire on the extent to which ESG legislation will impact on a firm's operations but also about what steps are being taken to comply with the rules. Again, do not expect insurers to just ask about the 'E'. It is recommended asset managers review the scope of their IMI liability insurance for investigations and investor-related disputes coverage arising from allegations of 'greenwashing' claims.

Key issues to watch

continued

Cybersecurity



Observation:

Cybersecurity remains a key risk focus around the world, with regulators and investors continuing their search for greater evidence that cybersecurity risk management policies and procedures have been implemented. This has only intensified in light of the Russian/Ukraine conflict and the possibility of a surge in cybers threats. All this when the availability of cyber insurance is in limited supply and traditional financial lines underwriters are in some cases trying to 'carve out' (exclude) certain cyber perils such as cyber extortion from tradition IMI policies as a consequence of the steep rise in ransomware activity.



Concern:

The FCA expects all financial institutions to be resilient upfront rather than thinking about it as an afterthought. Companies should consider this when reviewing existing technology or introducing new technology when managing cyber risks. We expect global regulators to continue to roll out cybersecurity related regulations to which managers will be required to adhere. The risk of being the subject of a cyber-attack coupled with the regulatory and investor scrutiny that may follow is firmly on the agenda of insurers.



Suggestion:

Firms should expect even more inquiries from insurers regarding the resiliency of the organisation's cybersecurity risk framework. Existing IMI policies should be reviewed for cyber coverage, including the scope and limitations of such cover and whether such cover has been 'affirmed' by insurers. If not, separate cyber policies should be sought. However, due to the limited number of insurers offering standalone cyber, do not expect this to be a cheap or easy task.

Russia and Ukraine



Observation:

The conflict has led to an unprecedented response from the USA, Canada, EU, UK and much of the Western world. The severity of the sanctions imposed on Russia and, to a lesser extent, Belarus to date, will and is already having major ramifications for international finance and trade around the world. Furthermore, the FCA **issued a reminder** recently saying it expects firms to have established systems and controls to counter the risk of being used to further financial crime. This includes compliance with financial sanctions obligations.



Concern:

The events in Ukraine have created compliance (i.e. sanctions), divestment, valuation and settlement challenges for the asset management community with exposure to Russian assets. These issues, combined with the potential for trading errors due to market volatility and potential investor claims arising out of negatively impacted investments, may lead to increased claims activity against asset managers. The FCA's statement is particularly relevant to those individuals who under the Senior Managers and Certification Regime (SMCR) have prescribed responsibilities relating to financial crime.



Suggestion:

Whilst firms will continue to undertake a holistic assessment of financial crime risks, for example, money laundering, sanctions evasion, terrorist financing and fraud, as the situation in Ukraine evolves, we expect insurers to ask more probing questions around internal controls and how these are updated/ documented/rolled out on an ongoing basis. We also expect insurers to seek confirmation of no direct exposure to Russia or Belarus, as well as other sanctioned territories.

Key issues to watch

continued

Special update - USA

While appreciating this market update is primarily aimed at UK asset managers, a large number will also be subject to SEC regulation, so the following section on the flurry of activity at the SEC will likely be of interest:



SEC proposed private fund rules



Observation:

Citing the need to enhance investor protection, the SEC proposed new **rules** requiring greater transparency from, and imposing additional reporting obligations upon, investment advisers to private funds. The rules would require:

- (i) Quarterly investor statements
- (ii) Private fund adviser audits
- (iii) Fairness opinions in adviser-led secondary transactions
- (iv) The prohibition of certain activities, including limiting or eliminating liability for adviser misconduct
- (v) The prohibition of preferential terms to certain investors regarding redemption rights and portfolio holdings if such information will have a material, negative effect on other investors.



Concern:

The rules would prohibit advisers from seeking reimbursement, indemnification, exculpation, or limitation of its liability by the private fund or investors for a 'breach of fiduciary duty, wilful misfeasance, bad faith, negligence, or recklessness in providing services to the private fund'.³ Such prohibitions may increase the risk of loss to the adviser's own balance sheet.



Suggestion:

We expect insurers to inquire about the impact such rules would have on an adviser, including the extent to which 'hedge clauses' are currently used in an effort to limit its liability to the funds and/or investors. As indemnification from the funds may no longer be available, advisers may wish to reconsider the limits it maintains under their IMI program, as well as its premium allocation methodology.

3. <https://www.sec.gov/rules/proposed/2022/ia-5955.pdf> - page 133

Key issues to watch

continued

SEC cybersecurity rules



Observation:

The SEC has proposed new cybersecurity **rules** under the Investment Advisers Act of 1940 and the Investment Company Act of 1940. Advisers and funds subject to the rule, which includes registered investment companies and business development companies, would be required to adopt and implement cybersecurity risk management policies and procedures and adhere to new cybersecurity incident reporting and disclosure requirements. Fund directors would be required to approve these policies and procedures, as well as any proposed material changes, and review reports on cybersecurity incidents.



Concern:

The SEC rules are the latest in an ever-growing patchwork of cybersecurity regulatory requirements that must be carefully navigated by asset managers and the boards of funds. The risks associated with running afoul of these regulations, combined with the spate of ransomware activity, has raised concerns amongst the underwriting community. We expect some insurers to continue to clarify policy wordings in an effort to clarify what is and is not covered under various IMI/fund D&O policies.



Suggestion:

Beginning early and engaging the appropriate internal subject matter expert(s) to address cybersecurity underwriting questions is key to this aspect of the renewal process. To the extent a cyber exclusion to the IMI policy is proposed, it is important to review the scope of such language and/or market the programme to alternative insurers willing to offer more favorable terms.





Contacts

For further information please contact

Henry Keville
Lead Relationship Manager (Asset Management)
+44 20 3124 6445
Henry.Keville@WillisTowersWatson.com

Susan Finbow
Global Head of FINEX Financial Institutions
+1 416 646 8294
Susan.Finbow@WillisTowersWatson.com

Heather Kane
US Head of FINEX Financial Institutions
+1 212-915-7905
Heather.Kane@WillisTowersWatson.com

Medina El-Farra
Team Leader, FINEX Financial Institutions
Medina.El-Farra@WillisTowersWatson.com
+1 416 646 3183

Martin Giggins
**Director, Singapore and Hong Kong -
FINEX Financial Institutions**
+1 212-915-7905
Martin.Giggins@WillisTowersWatson.com

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