Policy briefing

23 November 2016

Autumn Statement 2016

This briefing provides some background and high level analysis of the areas of the Chancellor's Autumn Statement that will be of interest to Chartered Insurance Institute members.

The note covers:

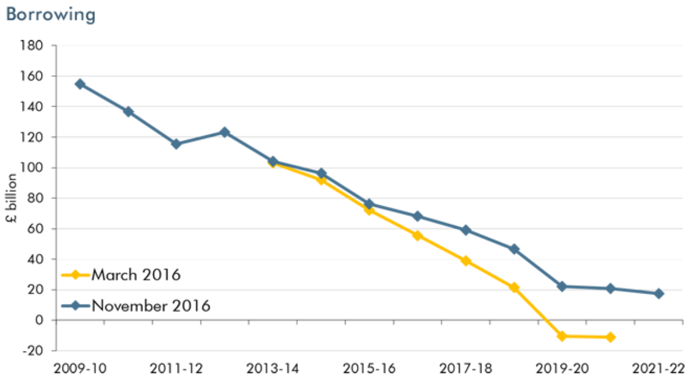
1. The background to the Statement
2. The 'Brexit factor'
3. The major announcements of interest to members:
    - Insurance Premium Tax (IPT)
    - Whiplash reform
    - Consumer insurance market
    - Insurance Linked Securities
    - FinTech
    - Corporation Tax
    - Supporting management skills
    - Pension scams
    - National Productivity Investment Fund
    - The triple lock on pensions
4. Stakeholder responses

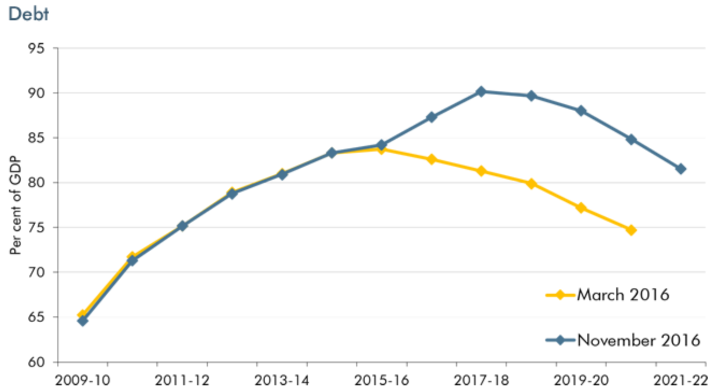
Chartered Insurance Institute statement in response to the announcement of a further increase in Insurance Premium Tax (IPT):

> **"It is very disappointing that the Government has for the third time in twelve months targeted insurance as a source of additional revenue for the Treasury without considering the unintended consequences this will have on the public's access to insurance. At a time when we are observing under-provision of insurance in many parts of society, effectively doubling insurance premium tax between Nov 2015 and June 2017 will have the effect of disproportionately increasing the cost of protection and further dissuading many people from managing the risks they face. The Government should remind themselves of the words of Sir Winston Churchill which are as relevant to our society today as they were a hundred years ago:**
>
> ***If I had my way, I would write the word 'insure' upon the door of every cottage […] because I am convinced for sacrifices so small, families and estates can be protected against catastrophes which would otherwise smash them forever*."**
>
> **Keith Richards, Managing Director (Engagement)**

Background

The Autumn Statement of 2016 was the first fiscal statement made by the new Chancellor of the Exchequer Philip Hammond since his appointment in July, and also the first under new Prime Minister, Theresa May. Hammond had informed cabinet colleagues that he was not intending to produce a 'rabbit out of the hat' during the speech - a conscious departure from the last minute surprises favoured by his predecessors George Osborne and Gordon Brown - but would instead deliver a sober fiscal statement that centred on medium-term market stabilisation, against the backdrop of a more subdued outlook for economic growth as the UK negotiates a new relationship with the EU.



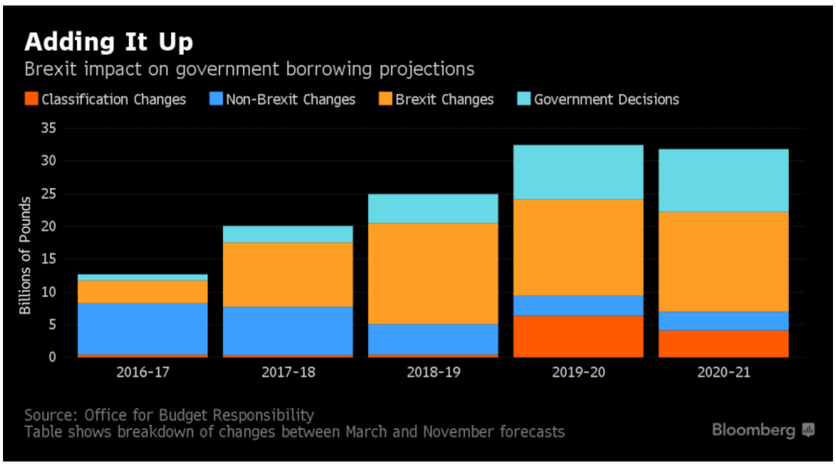


Source: Office for Budget Responsibility 'Economic and fiscal outlook'

According to the forecasts published by the independent Office for Budget Responsibility on the day of the Statement, real GDP will expand by 1.4% in 2017, weaker than the 2.2% prediction made in March. Similarly the GDP forecasts for 2018 were also revised down from 2.1% to 1.7%. The OBR also anticipate that this slower economic growth will result in tax revenue that is £15bn lower by 2020 than was previously expected – contributing to an estimated additional £122 bn of net borrowing it predicts the Government will need to secure through to 2021.

The Brexit factor

The OBR's 'Economic and fiscal outlook' also contained the UK's first official forecast of the costs of the EU referendum result to the UK. The analysis attributed £58.7 bn of the additional £122 bn of net borrowing required through to 2021 to charges relating to the UK's withdrawal from the EU. The extra costs will peak in 2018-19, as the U.K.'s proposed two-year exit process draws to an end.



While the economy has so far proved more resilient to the UK's decision to leave the EU than many economists predicted, the OBR analysis ascribes the majority of Brexit-related costs to an anticipated slow down in the pace of import and export growth due to the negotiation of trading arrangements, the adoption of a tighter migration regime than that is currently in place, uncertainty for firms leading to some investment being postponed or cancelled and the fall in the pound squeezing household real incomes by increasing consumer prices and halting real earnings growth.

Controversially, the amended growth and borrowing forecasts are similar to the projections made before the referendum by then Chancellor George Osborne: principally that the public finances would take a £30 bn hit if the UK voted to leave the EU. The OBR now predicts the UK will have to borrow £21.9 bn in 2020, compared with the £10.4 bn surplus predicted in March.

Major announcements

Philip Hammond's first Autumn Statement was also his last. In future there will only be one major fiscal announcement a year, which will be an Autumn Budget, in addition to a Spring Statement that responds to OBR forecasts as mandated - but with no major new announcements. Acting on the OBR forecasts, the Chancellor conceded that the Government was no longer on course to achieve a budget surplus during the current Parliament, and would instead preside over a significant loosening of existing fiscal targets to provide the 'headroom' for almost £56 bn (2.5% of GDP) more structural borrowing in 2020-21 than his predecessor was aiming for in March. Three new rules as part of a new fiscal framework were revealed:

1. To balance the books "as soon as is practicable" in the next Parliament and cut the deficit to less than 2% by 2020
2. Net debt as a share of GDP should be falling by the end of this Parliament
3. Welfare spending must be within a "realistic" cap.

Insurance Premium Tax (IPT)

The standard rate of Insurance Premium Tax will rise from 10% to 12% from 1 June 2017. IPT is a tax on insurers and so any impact on premiums depends on insurers' commercial decisions. It is the third rise since the Summer Budget in 2015, when the former Chancellor George Osborne announced an increase from 6% to 9.5% which came into effect in November last year. The rate was increased again to 10% in this year's March Budget, coming into effect on October 1st. The third to 12% means the tax has doubled in less than 18 months.

IPT affects more than 50 million policies and applies to those purchased by businesses, charities and individuals. Taken together, the three rises will raise over £13 bn for the Government over five years.

Whiplash reform

The Ministry of Justice is consulting on proposals which will reduce the unacceptably high number of whiplash claims and allow insurers to cut premiums. The Government will bring forward supporting legislation in the Justice Bill and expects insurers to pass on savings which average around £40 for drivers in England and Wales, worth a total of £1 bn.

Consumer insurance market

New FCA rules on consumer insurance policy renewals, being introduced in April 2017, will encourage consumers to shop around instead of renewing their policy automatically. The FCA will monitor the effect of the rules and the Government will ask the FCA to consider further intervention if necessary.

Insurance Linked Securities

The Government is consulting on a new regulatory and tax framework for Insurance Linked Securities. Alongside this the Prudential Regulatory Authority (PRA) and Financial Conduct Authority (FCA) will consult on their approach to the authorisation and supervision of Insurance Special Purpose Vehicles. This will help to maintain London's position as the most important global hub for reinsurance business. The Government will place final regulations before Parliament in the spring.

FinTech

To support investment in UK FinTech, the Department for International Trade will provide £500,000 a year for FinTech specialists. The Government has also commissioned an annual 'State of UK FinTech' report on key metrics for investors, and will also launch a network of regional FinTech envoys. Ministers have agreed with the Joint Money Laundering Steering Group that they will modernise their guidance on electronic ID verification to support the use of technology to access financial services.

Corporation Tax

The decision was made to retain the already scheduled reduction in the rate of corporation tax to 17% by April 2020 – well below the OECD average of 24.85%. This further enhances the UK's competitiveness compared to the other G20 countries.

The Statement took aim at tax avoidance, as a new penalty is to be introduced for assisting tax avoidance as well as the avoiders themselves. Tax avoiders will also be unable to claim as a defence against penalties that relying on non-independent tax advice is taking reasonable care.

Supporting management skills

The government will provide £13 million to support firms' plans to improve their management skills by implementing Sir Charlie Mayfield's review of business productivity.

Pension scams

The Government will shortly publish a consultation on options to tackle pension scams, including banning cold calling in relation to pensions, giving firms greater powers to block suspicious transfers and making it harder for scammers to abuse 'small self-administered schemes'.

National Productivity Investment Fund (NPIF)

A new National Productivity Investment Fund will add £23 bn in high-value investment from 2017-18 to 2021-22. The Government will target this spending at areas that are critical for productivity: housing; research and development (R&D); and economic infrastructure. The NPIF will take total spending in these areas to £170 bn over the period from 2017-18 to 2021-22, reaching 1.7% of GDP in 2021-22. The new spending includes:

1. £7.2 bn to support the construction of new homes, including spending by Housing Associations
2. £4.7 bn to enhance the UK's position as a world leader in science and innovation
3. £2.6 bn to tackle congestion and ensure the UK's transport networks are fit for the future
4. £0.7 bn to support the market to roll out full-fibre connections and future 5G communications. The Government will encourage private investment with £400 million from the British Business Bank to unlock £1 bn of new investment in innovative firms planning to scale up, and a doubling of capacity to support exporters through UK Export Finance.

On the triple lock on pensions

The Chancellor said 'as we look ahead to the next Parliament, we will need to ensure we tackle the challenges of rising longevity and fiscal sustainability…'

Stakeholder responses

British Association of Insurance Brokers (ABI) 'Yet another increase in Insurance Premium Tax is a hammer blow for the hard pressed.' http://bit.ly/2fcfJMU

British Insurance Brokers' Association (BIBA) 'Over the past 15 months, policyholders have already seen an increase of 66% in the Insurance Premium Tax (IPT) they pay – this further increase to 12% in this regressive tax is outrageous and is a tax on protection which will hit everyone and especially those 'just about managing'. http://bit.ly/2fWiMrQ

Aviva 'You could say this is a tale of two governments: on the one hand, the Government plans to reduce the cost of motor insurance through whiplash compensation reforms which will save motorists around £40 - £50 a year; on the other hand, we're surprised by the announcement to increase the cost of insurance for a third time, which effectively doubles the amount of tax paid on insurance purchases in less than two years.' http://bit.ly/2fchQQH

PricewaterhouseCoopers (PwC) 'Consumers can expect to save around £40 on their car insurance premiums following government plans to cut compensation for whiplash injuries. However, we expect the same premiums to rise by £25 due to IPT rises put in place since October 2015. We expect further rises for IPT in coming years, which would further eat into any savings brought about through whiplash reforms' http://bit.ly/2fWi79P

Ernst & Young (EY) 'Reforms to whiplash claims will be welcome when they come in, but motorists are unlikely to see any cost savings until 2018.' http://bit.ly/2gqvbT2

TheCityUK 'Today's announcements should help to bring greater market stability, while emphasising the fact that Britain remains open for business.' http://bit.ly/2fcgyFs

Links

Government Autumn Statement policy paper: http://bit.ly/2gqvWvd

The Chancellor's Autumn Statement speech in full: http://bit.ly/2gENhUc

The OBR forecast: http://bit.ly/2fr2UwH and supporting documents: http://bit.ly/2foxqUG

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