

Reinsurance

M97/P97 2017–18 edition

Web update 01: 17 March 2017

Please note the following update (amendments in **bold** type) to your 2017-18 edition of the **M97/P97** study text.

Chapter 7, section D10H, page 7/37

Please add the following activity at the end of the section:

Activity

See chapter 11, section B4B to find out about the new discount rate. Consider the immediate impact of its implementation on a reinsurer's approach to reserving for personal injury claims in the context of a non-proportional treaty containing the example clause set out above.



Chapter 11, section B4B, page 11/8

Please add the following at the end of the section:

- **Discount rate.**

Discount rate

The discount (or 'Ogden') rate applies to the process by which damages paid to seriously injured individuals, in relation to future losses and expenses, are adjusted to reflect the fact that those damages are received in advance of the losses and expenses being paid because the funds are invested to generate a return.

On 27 February 2017, the Lord Chancellor announced changes to the discount rate used to calculate personal injury claims. It has been reduced from 2.5% to -0.75%, with effect from 20 March 2017. This implies that the Government expects that a claim recipient investing the damages settlement over their remaining life would get a negative return on investment, and the insurer must top up the expected loss.

This issue is of particular interest to liability and motor insurers. The change in discount rate will inflate the cost of lump sum payments made to claimants by insurers. The cost of this change is likely to be met primarily by the reinsurance industry as motor insurers and most liability insurers will have reinsurance protection. However, in the longer term reinsurance premiums will rise and the cost of this increase will be passed down to policyholders.

The change in discount rate means that insurers and reinsurers need to quickly reassess their reserves. This is likely to entail a thorough review of each claim file where third parties are claiming for future losses and applying the new discount rate which will result in significant increases to reserves.

You are encouraged to keep up with developments in this area as they arise.

