

LONDON MARKET FORECAST 2018

January 2018

The wealth of experience and expertise of the London Market defines its place as a forerunner in the global insurance market.

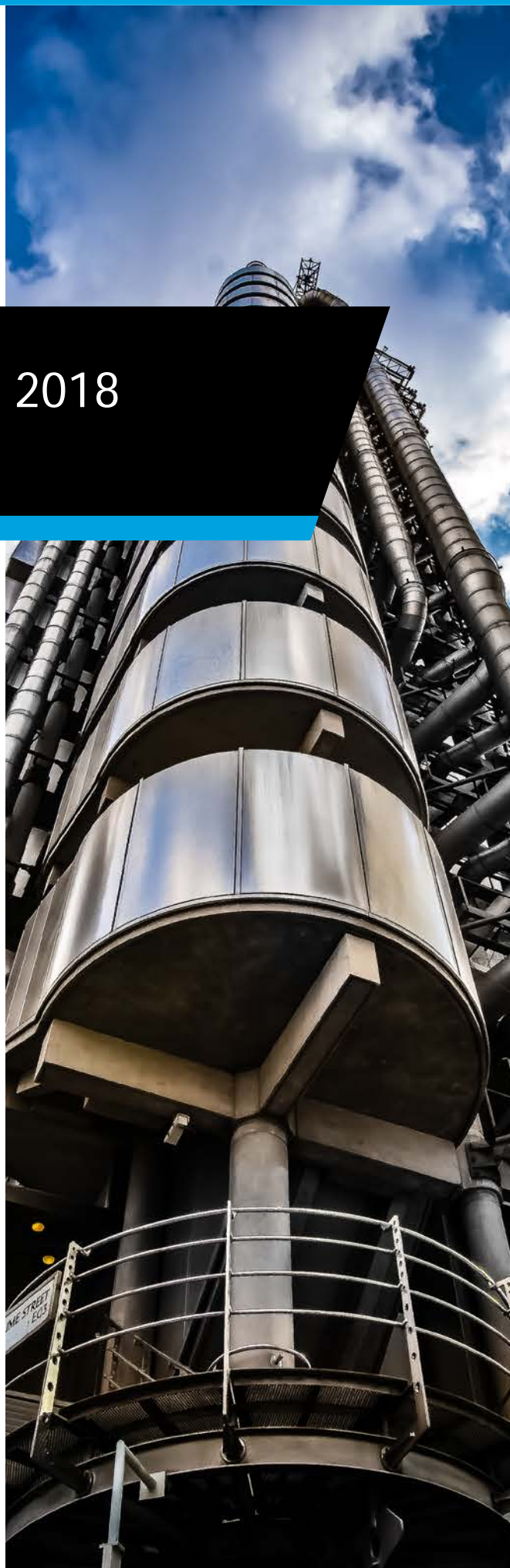
In order to preserve the benefits of its structure and creative approach to offering solutions, understanding potential market disruptors is becoming increasingly important. Indeed, anticipating changing risk perceptions is vital to its survival - especially where such perceptions are changing more quickly than was perhaps anticipated, most notably as a result of new technologies.

Political, business, environmental and societal drivers are also key to any forecast. As the shifting sands underpinning the market landscape promise to maintain their momentum during 2018 and beyond, we offer our predictions on some of the priority areas.

BACKGROUND

New technologies touch on every aspect of the London Market - from the claims data that the Internet of Things produces to help evaluate risk to the introduction of the Lloyd's Market Target Operating Model initiative.

Technology and, in particular, new approaches to coding and development may offer some of the answers to keep insurance products relevant and even offer the potential for transformation in both insurance and legal sectors. Assessment and evaluation of business practice to utilise these technological advances in investment decision making should be at the top of any business agenda.



The 2017 Autumn Statement and Industrial Strategy placed technology and innovation at the centre of the domestic political framework - confirming their status as tools to allow the UK to be at the forefront of emerging technologies, as well as the regulatory frameworks needed in support. While law reform projects to support cutting edge technological innovation will continue, the reality is that maintaining a political energy for much else other than Brexit may not be easy.

It waits to be seen what impact John Glen MP makes as new City Minister. Taking on responsibility for the overall strategic relationship with the UK financial services sector, including insurance, it is hoped that Glen will show a willingness to engage constructively with the industry and help champion it.

2018 will be a busy year for reviewing business practice. Important **regulatory reforms** that will touch the Market include the General Data Protection Regulation, which will take effect on 25 May 2018 and mean increased compliance requirements for business.

The requirements of the EU wide Insurance Distribution Directive will also be felt - in order to meet the FCA's desire to create the most mature conduct regulatory framework in Europe. While the European Commission has proposed delaying implementation to 1 October 2018, firms will need to ensure compliance by the application date specified in the final rules (depending on the outcome of the proposed delay).

We can also hope to see what impact the Insurance Act and the Enterprise Act will have on the insurance market, both in terms of how insurance is placed and how insurers deal with claims made by business - therefore adding to the claims horizon.

Against this background, we consider other key areas for the London Market in 2018:

CYBER

One issue that could become more prominent in 2018 is so-called "short-firm fraud", where fraudsters mock-up emails to pass themselves off as employees of a legitimate company and obtain goods on credit from the insured. The insured thinks they are dealing with a legitimate company and agree to deliver goods to a depot before payment is made. When the insured chases up payment, they find that the legitimate company has no knowledge of the order and refuses to pay.

The losses flowing from these scenarios are not usually covered under standard cyber policies. However, many insureds (and some brokers) assume they are as the

fraud usually involves fake emails, so there appears to be a "cyber" element. This leads to a number of unnecessary notifications to insurers and inevitably leads to coverage challenges and complaints to underwriters about the scope of cover.

This issue is becoming increasingly common, especially amongst small independent IT hardware resellers. In light of this, some cyber underwriters are looking to tighten up cyber policy wordings to make it absolutely clear that cover is not provided for first party losses that arise out of social engineering frauds. Education and communication between insurers, brokers and insureds on the scope of coverage under cyber policies may assist all parties involved.

AVIATION

Research indicates a potential knowledge gap in the market, particularly regarding current and proposed legislation. This gap will have to be addressed quickly. The market needs to understand the risks posed by drones in all potential areas - including aviation, general insurance, marine, product liability, cyber and privacy.

Policies with drone exposure will have to cover the strict liability of the operator of an aircraft - which includes drones. The relationship with current liability regimes and defences available and the new drones legislation is, as yet, unknown but could alter how we interpret current standard terms, legislation and conventions.

Due to the government's desire for the UK to become world leaders in this field, it is anticipated that the development of UK drone legislation will progress quickly (other legislative demands aside) in 2018. The detail of this legislation will need to be considered carefully, as both insurers and their customers will feel its impact. One well-known camera maker has already left the consumer drone market, citing 'a hostile regulatory environment' as having a negative impact on the future of the drone market.

PRODUCT LIABILITY

Judgment in the Pinnacle Metal on Metal Hip Group Litigation is expected around late spring 2018 in what is anticipated to be one of the most important decisions in the field of product liability in over 15 years. The judgment is likely to clarify the legal basis on which a determination as to defect should be made, and will therefore have implications generally for manufacturers and distributors working in the medical devices and pharmaceutical industries.

It is alleged that the Pinnacle metal hip prostheses produced by DePuy (represented by Kennedys) are defective. Liability and causation are being tried as preliminary issues, DePuy having advanced the group action for determination ahead of group claims against various other manufacturers.

MARINE

In 2017, a shipping blockchain system was piloted which will be used to process approximately 10 million containers this year. We suspect the marine transport sector, in particular, will continue to exploit the potential of blockchain technology.

The ability to enable multiple parties to share and verify data and documents in real time will revolutionise the transport industry. Carriers will save money; risk and liability data will be captured more efficiently; transactions and claims payments will be processed even quicker. In light of these changes, insurers will need to think about the data they require and how that data is shared. The development of blockchain is likely in itself to be the precursor for further change. Standard marine practice will inevitably evolve.

Marine insurers should keep a close eye on how the market and legislation adapts with the advances in autonomous technology - the implications arising from hacking into a drone or car can be directly compared to the risks involved with autonomous vessels.

CONSTRUCTION

2018 is going to be all about the construction industry in a post-Grenfell and post-Carillion era. There will be a greater scrutiny of construction projects in general, including the value engineering process and the need for a detailed review of Building Regulations (already instigated by the Home Secretary).

In addition, mental health has been highlighted as a growing issue and may increasingly make its way to boardroom level. One theory is that, since the Brexit decision, some construction companies have scaled back operations which has led to an increase in stress related litigation. If that is right, an increase in EL claims related to stress and other such issues may follow.

Brexit is, of course, not the only factor having a negative impact on this sector. Continued growth is not guaranteed and job security - whether with the primary or sub-contractor - is of genuine concern. These fears are echoed across numerous business sectors. Therefore, might the uncertainty and instability of the UK economy, generally, prompt an increase in claims relating to mental health more widely?

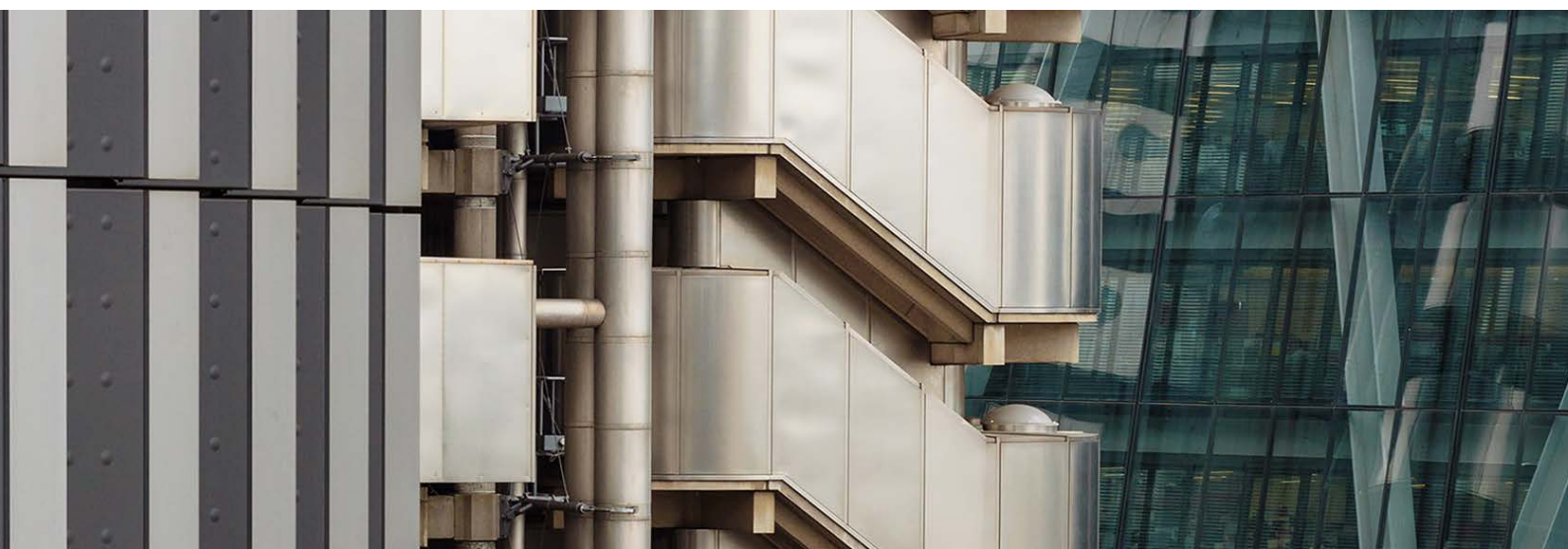
PROPERTY DAMAGE AND RECOVERIES

The 2017 hurricane season had a devastating impact on property owners and insurers. The future impact of such a prolific year reaches beyond the likely increase in premiums. The damages sustained highlighted flaws in the present process, such as ineffective hurricane plans attached to yacht insurance applications. The losses also identified vulnerable markets for insurers and this could lead to a reduction in available cover for insureds, particularly when the scientific consensus seems to be that 2017's hurricane activity may be the new norm, rather than the exception.

ENVIRONMENTAL LIABILITY

As the impact of climate change continues to be felt around the world, the frequency of both direct claims and related litigation is increasing.

Classes of businesses particularly exposed include general and public liability, directors' and officers' liability and professional indemnity insurance. The insureds at risk also extend beyond the obvious, such as oil and gas companies. Last year, minority shareholders



in the Commonwealth Bank of Australia (CBA) issued proceedings alleging failures by CBA to disclose risks associated with climate change to their shareholders, and probing CBA's association with a controversial coal-mining project.

Even with powerful voices questioning the effect or existence of climate change, we anticipate that an increase in the number and the type of dispute is likely.

PROFESSIONAL AND FINANCIAL LINES

How cyber breaches are handled continues to offer a potential increase of claims against directors and officers. Other factors that could generate claims activity in this space include:

- Tax relief schemes - as HMRC's powers are extended both primary and secondary claims could increase.
- Political uncertainty - including Brexit and the perceived threat of taxation changes to property, the 'top earners' and corporates.
- Legislation and regulation - the likely extension of the FCA's Senior Managers Regime, the expansion of anti-corruption legislation, the introduction of the Criminal Finance Act and the new reporting requirement introduced by the Modern Slavery Act.

FURTHER INFORMATION

To find out more about our services and expertise, and key contacts, go to: kennedyslaw.com

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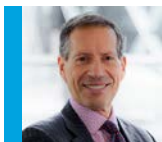
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