



Guernsey Financial  
Services Commission

# **APPROVED ASSETS REGULATION CONSULTATION**

**A CONSULTATION PAPER ON THE REVISION OF  
REGULATIONS FOR LICENSED INSURANCE MANAGERS AND  
INTERMEDIARIES**

**Issued 10<sup>th</sup> May 2018**

This Consultation Paper makes proposals in respect of the Regulations applicable to Insurance Managers and Insurance Intermediaries (together referred to as “Licensees” for the purposes of this Consultation Paper) licensed under the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002 (“the Insurance Managers and Intermediaries Law”).

The Guernsey Financial Services Commission invites comments on this Consultation Paper and your comments should be submitted by no later than 18<sup>th</sup> June 2018.

Responses should be sent to:

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## Proposed Amendments to the Insurance Managers and Insurance Intermediaries (Approved Assets) Regulations, 2002

1. The Guernsey Financial Services Commission (the “Commission”) is proposing that the Insurance Managers and Insurance Intermediaries (Approved Assets) Regulations, 2002 (“the Regulations”) should be revised.
2. The key aim of this revision is to remove a current gap in the existing prudential rules for Licensees, which has the effect at present of weakening the quality of regulatory capital available to Licensees.

### Background – Current Minimum Capital Requirement for Insurance Managers and Insurance Intermediaries

3. Pursuant to section 4(2)(h)(iii) of the Insurance Managers and Insurance Intermediaries Law, Licensees are required to maintain Shareholders’ Funds of an amount equal to or exceeding the Minimum Capital Requirement (the “MCR”). Pursuant to Schedule 3 of the Insurance Managers and Insurance Intermediaries Law, this is an amount determined by the Commission from time-to-time.
4. Schedule 3 of the Insurance Managers and Insurance Intermediaries Law also states: *“‘shareholders’ funds’ means the value of the excess of a licensee’s assets over its liabilities; and for the purposes of this definition the expression ‘liabilities’ excludes share capital, retained reserves and loans from shareholders where they are subordinated, in writing, to the prior claims of all other creditors”*.
5. The Minimum Capital Requirement for Licensed Insurance Managers and Insurance Intermediaries, which was issued by the Commission and subsequently came into force on 12<sup>th</sup> March 2009, defines the MCR and the formula for its calculation. The MCR for Licensees is set as the higher of £25,000 or 125% of the Licensee’s professional indemnity insurance deductible or excess. The formula used to determine whether the Licensee maintains the MCR is the total of the Approved Assets minus the total liabilities of the Licensee.
6. Pursuant to regulation 1 of the Regulations, Approved Assets are defined as those assets held by the Licensee and valued in accordance with Recognised Accounting Standards (as defined in the Insurance Managers and Insurance Intermediaries Law) less those assets held which are designated as Unapproved Assets.
7. Unapproved Assets are further defined pursuant to regulation 2 of the Regulations as:
  - a) Positive goodwill, being the value of a business in excess of the quantified value of its other assets and liabilities;

- b) Fixtures and fittings, being any furniture or other non-structural items owned by the licensee;
  - c) Computers and information technology equipment, which include any device used for the storage or processing of data electronically; and
  - d) Motor vehicles, being any car, truck, motorcycle, or other vehicle that can be used to transport persons or goods and is of a type permitted to travel on public roads.
8. An illustrative example summarising the calculation of the current capital requirements for Licensees, using hypothetical values, can be seen as follows:

<b>Illustrative Purposes Only</b>	<b>£</b>	<b>£</b>
<i>Net Approved Assets Calculation</i>		
Fixed Assets	5,000	
Loan to Shareholder	50,000	
Trade & Other Receivables	35,000	
Cash & Cash Equivalents	10,000	
<b>Total Assets</b>		<b>100,000</b>
<i>Less: Unapproved Assets</i>		<i>(5,000)</i>
Trade & Other Payables	(10,000)	
Subordinated Shareholder Loans	(10,000)	
<b>Total Liabilities</b>		<b>(20,000)</b>
<i>Add Back: Subordinated Shareholder Loans</i>		<i>10,000</i>
<b>Net Approved Assets</b>		<b>85,000</b>
<i>MCR as the higher of:</i>		
£25,000 Floor	25,000	
125% of PII Deductible / Excess	55,000	
		<b>(55,000)</b>
<b>Excess / (Deficit) against MCR</b>		<b>30,000</b>

Total assets of £100,000 are adjusted to deduct Unapproved Assets. The only Unapproved Assets of the example firm are £5,000 of fixed assets. Under the current form of the Regulations, the £50,000 loan owed to the firm by a shareholder is counted as an Approved Asset.

Total liabilities of £20,000 are then deducted from this. The firm in this example has received a loan from a shareholder, which is subordinated to all other creditors. This is therefore added back, as it is instead counted towards shareholders' funds. This leaves net approved assets of £85,000 under the current Regulations. This is compared to the MCR of £55,000 to determine if the hypothetical firm above has maintained the MCR.

### Proposed Amendments to the Regulations

9. In reviewing the definition of Unapproved Assets, the Commission has identified a gap in the current regulatory capital framework. Loans receivable from owners, or other associated parties, are considered Approved Assets under the Regulations. This enables an owner or associated party to capitalise a Licensee and subsequently loan this capital back.
10. This has the potential effect of significantly weakening the regulatory capital available to the Licensee.
11. It is therefore proposed that the Regulations be amended to include loans to, or other debts owed by, associates, associated parties and controllers of the Licensee within the definition of Unapproved Assets.
12. Given the range of circumstances surrounding such associated party loans that has been observed by the Commission in practice, it is also proposed that the Regulations be amended to allow the Commission to approve in writing the designation of certain loans, or other debts owed by, associates, associated parties and controllers of the Licensee as Approved Assets. This would enable the Commission to assess specific features, such as guarantees over or collateral for such loans, on a case-by-case basis where necessary.
13. It should be emphasised that under the proposed amendments loans could continue to be made to controllers, associates and associated parties with the proportion of assets not required to meet the MCR calculation. A draft form of the proposed amendments to the Regulations is included in an appendix to this Consultation Paper.

### Impact Assessment

14. In proposing the amendment to the Regulations noted above, the Commission has undertaken an assessment of the potential impact of these changes on affected Licensees.
15. The Commission's assessment has been conducted by way of scenario analysis. This has been done by reducing the level of Approved Assets by the amounts due to controllers, associates and associated parties for affected Licensees. This has been based on values taken from the latest audited financial statements submitted by Licensees, as part of the latest annual return received by the Commission, that were available as at the date of this Consultation Paper.
16. The results of the impact assessment suggest that a few Licensees will be affected by this amendment. The Commission has contacted the affected Licensees to discuss the amendment prior to the consultation process. The Commission is of the view that the changes required because of the amendment can be managed effectively.

### Timetable

- 17.** Responses to this Consultation Paper are sought by Monday 18<sup>th</sup> June 2018.
- 18.** Following this consultation period, the Commission will evaluate and collate the responses and will issue feedback on the comments received together with the resulting relevant new and amended regulations in July 2018.
- 19.** The Commission will implement the amended Regulations on either their issuance or following a three-month transition period. This will be determined based on feedback received from Licensees as part of the consultation process.

**Appendix: The Insurance Managers and Insurance Intermediaries (Approved Assets) (Amendment) Regulations, 2018**

# **The Insurance Managers and Insurance Intermediaries (Approved Assets) (Amendment) Regulations, 2018**

*Made*

*Coming into operation*

*Laid before the States*

THE GUERNSEY FINANCIAL SERVICES COMMISSION, in exercise of the powers conferred upon it by section 61A of the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002, and after consultation with the States of Guernsey Policy & Resources Committee, the States of Alderney Policy and Finance Committee and the Chief Pleas of Sark General Purposes and Finance Committee, hereby makes the following regulations:-

## **Amendment.**

1. Regulation 1 of the Insurance Managers and Insurance Intermediaries (Approved Assets) Regulations, 2008, shall be amended as follows:

The full-stop at the end of Regulation 1 shall be removed and replaced with “, unless otherwise permitted by the Commission.”

2. Regulation 2 of the Insurance Managers and Insurance Intermediaries (Approved Assets) Regulations, 2008, shall be amended as follows:

The word “and” shall be removed from the end of subparagraph (c).

The full-stop at the end of sub-paragraph (d) shall be replaced with “, and”.

The following subparagraph shall be inserted immediately after subparagraph (d):

“(e) subject to the Commission directing otherwise, loans to, or other debts owed by, associates, associated parties or controllers of the licensee.”

## **Interpretation.**

3. (1) Any reference in these Regulations to an enactment or Regulation is a reference thereto as from time to time amended, repealed and replaced, extended or applied.  
(2) The provisions of the Interpretation (Guernsey) Law, 1948 shall apply to the interpretation of these Regulations throughout the Bailiwick of Guernsey.



**Citation.**

4. These Regulations may be cited as the Insurance Managers and Insurance Intermediaries (Approved Assets) (Amendment) Regulations, 2018.

**Commencement.**

5. These Regulations shall come into force on