

Rules for Special Purpose Insurers

Closed 11 Nov 2016

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Contact

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Overview

During October and November 2016, the Commission consulted on proposals to amend the framework underlying the Insurance Business (Bailiwick of Guernsey) Law 20002 with the making of rules for Special Purpose Insurers and a related, minor amendmetns to the Insurance Business (Solvency) Rules 2015.

Related

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Guernsey Financial
Services Commission

INSURANCE BUSINESS (BAILIWICK OF GUERNSEY) LAW, 2002
CONSULTATION PAPER ON RULES FOR SPECIAL PURPOSE
INSURERS

Issued 14 October 2016

The Guernsey Financial Services Commission invites comments on this consultation paper and your comments should be submitted by no later than 11 November 2016.

Responses should be sent to:

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The Commission is consulting on proposals to amend the framework underlying the Insurance Business (Bailiwick of Guernsey) Law 2002 (the “Law”) with the making of rules for Special Purpose Insurers and a related, minor amendment to the Insurance Business (Solvency) Rules 2015.

In making these proposals the Commission is responding to requests from industry, who believe that distinct rules for Special Purpose Insurers (“SPIs”) will assist in attracting Insurance Linked Securities business such as collateralised catastrophe reinsurance to the Bailiwick.

The proposed Insurance Business (Special Purpose Insurer) Rules 2016 (the “Rules”), which are provided in Annex 1 to this document, define a Special Purpose Insurer class of insurer.

SPIs may include certain types of insurance linked transactions business in Guernsey, including collateralised reinsurance, catastrophe bonds, side-cars and life based securitisations. SPIs must be fully collateralised to the extent of their liabilities, meaning that, unlike traditional insurers, they carry no risk gap between their liabilities and assets. Typically, cash assets will be applied against liabilities, however the Commission recognises that the commercial intentions of counterparties may be satisfied by the use of (re)insurance, letters of credit, or partly paid shares and the Commission may apply its discretion to approve the use of such assets (or a combination of them). When considering approval of the use of contingent assets the Commission will take into account the regulatory status, regulatory domicile, financial credit rating of the counterparty and any other information it deems relevant.

The proposed Rules also provide for application to the Commission by an established SPI structure to grant a single consent for the formation of further Special Purpose Insurer cells, whether generally or limited in extent, without further or additional application to the Commission, subject to certain conditions. These proposed provisions formalise current discretionary practice of the Commission under the Insurance Business (Licensing) Regulations, 2010.

It is further proposed that the Insurance Business (Solvency) Rules 2015 (the “Solvency Rules”) be amended to expressly include a SPI within the definition of a Category 6 insurer. As a Category 6 insurer, a SPI would not be required to maintain the Minimum Capital Requirement, Prescribed Capital Requirement or to conduct an Own Risk and Solvency Assessment. The proposed amendment to the Solvency Rules is described in Annex 2.

If approved it is proposed that the Rules will come into effect on 1 January 2017.

The Commission invites comments from all interested parties on the proposal as outlined in this document and the Annexes.

ANNEX 1

DRAFT

**THE INSURANCE BUSINESS (SPECIAL PURPOSE
INSURER) RULES 2016**

Introduction

- 1) The Guernsey Financial Services Commission (the “Commission”), in exercise of the powers conferred upon it by Sections 38A and 38B of the Insurance Business (Bailiwick of Guernsey) Law, 2002, as amended and of all other powers it enables, hereby makes the following rules:–

Citation

- 2) These rules may be cited as the Insurance Business (Special Purpose Insurer) Rules, 2016.

Commencement

- 3) These rules shall come into force on 1 January 2017.

Status

- 4) These rules shall have the status of rules of the Commission under the provisions of section 38A of the Insurance Business (Bailiwick of Guernsey) Law, 2002 (the “Law”), as amended.

Definitions

- 5) The defined terms used in these Rules shall be defined as follows;
 - a) “Acceptable Rating Agency” means a rating agency prescribed in Schedule 5 of the Insurance Business (Solvency) Rules 2015.
 - b) “Law” means the Insurance Business (Bailiwick of Guernsey) Law, 2002, as amended.
 - c) “Special Purpose Insurer” means an insurer or a cell of a protected cell company which conducts insurance business and is a Fully Funded Special Purpose Insurer funded from the proceeds of any one or more of the following;
 - i) a debt or equity issuance whereby the repayment rights of the providers of such debt or security are subordinated to the rights, liabilities or contractual obligations of the person insured; or
 - ii) some other financing mechanism approved by the Commission.
 - d) “Fully Funded Special Purpose Insurer” means an insurer or cell which satisfies all of the following requirements:
 - i) the insurer or cell has at all times assets the value of which is equal to or exceeds the aggregate maximum risk exposure and the insurer or cell is able to pay the amounts it is liable for as they fall due;
 - ii) the proceeds of the debt or equity issuance or other financing mechanism are:
 - (1) fully paid-in; or

- (2) in the form of contingent assets where the finance provider has achieved a financial rating (counterparty, credit or financial strength as applicable) of at least A- as of the date of application and as determined by an Acceptable Rating Agency;
 - iii) according to the terms of such financing mechanism, the rights of participants in any such mechanism are subordinated to the claims of creditors under the contracts of insurance;
 - iv) the insurer or cell only enters into contracts or otherwise assumes obligations or contingent liabilities which are solely necessary for it to give effect to the purposes set out from time to time in its agreed business plan; and
 - v) to the extent that more than one insurance contract is in place within the insurer or cell, each of the insurance contracts is structured so that the insurer or cell meets the fully funded requirements, as described in this definition, individually for each contract.
- e) "Qualified Investor" means:
- i) a Government, local authority, public authority or supra-national body (in the Bailiwick or elsewhere); or
 - ii) a person, partnership, unincorporated association or body corporate which has total assets of £5 million;
 - iii) Guernsey registered or authorised collective investment schemes; or
 - iv) a company quoted on an investment exchange licensed by the Commission or a Recognised Investment Exchange.
- f) "Recognised Investment Exchange" means a recognised investment exchange as defined under the Protection of Investors (Bailiwick of Guernsey) Law, 1987.
- g) "Type 1 letter of credit" means a Type 1 letter of credit as defined in the Insurance Business (Solvency) Rules 2015 as amended.
- h) Unless otherwise defined in these rules, terms used in these rules that are defined in the Law shall have the meaning given to them in the Law.

Controllers, Collateral & Participation

- 6) Special Purpose Insurers may only raise capital for underwriting;
- a) From Qualified Investors (whether via subscription for or purchase of debt or equity instruments or otherwise);
 - b) By listing of securities (whether debt, equity or derivative instruments) issued by the Special Purpose Insurer on an investment exchange licensed by the Commission or a Recognised Investment Exchange; or
 - c) By such other means or from such other persons as may be approved in writing from time to time by the Commission.
- 7) The capital utilized for underwriting by a Special Purpose Insurer may include the following contingent assets approved by the Commission on a case by case basis:

- a) Type 1 letters of credit
- b) Reinsurance
- c) Partly paid shares

Applications, Consents and Requirements

- 8) An applicant for either the licensing of a new insurer or the creation of a new cell which meets the definition of a Special Purpose Insurer shall notify the Commission within the relevant application of its status as a Special Purpose Insurer and shall provide such information as the Commission may deem necessary to demonstrate compliance with the content of these Rules, the Law and any associated rules, codes, ordinances or regulations.
- 9) Upon application by a protected cell company the Commission may grant a single consent for the formation of further Special Purpose Insurer cells, whether generally or limited in extent, without further or additional application to the Commission, provided that such permission is subject to the following conditions:
 - d) that the business of such initial and further cell or cells complies and will continue to comply at all times with the terms and limits of the business plan submitted to the Commission under section 11 of the Law and with the content of these Rules;
 - e) that the ownership of such further cell or cells will be restricted to owners of a cell or cells of the Special Purpose Insurer previously approved by the Commission; and
 - f) that, within seven calendar days of the effective date of insurance, the General Representative of the Special Purpose Insurer shall notify the Commission and provide the Commission with:
 - i) a completed application form in such form as the Commission may prescribe;
 - ii) a narrative business plan;
 - iii) the relevant fee; and
 - iv) confirmation of the effective date of insurance.
- 10) The authorisation of at least one Guernsey resident signatory is required for all bank payments made by a Special Purpose Insurer.

ANNEX 2

Draft Amendment to paragraph 6 of the Insurance Business (Solvency) Rules 2015

Existing text:

(f) Category 6 - Special Purpose Entities - entities that the Commission agrees in writing may fall into this category. This is primarily intended for insurer's whose underwriting and counterparty credit risk are effectively eliminated - examples of these would include transformer cells, fully collateralised catastrophe cells, ILS cells and fully funded entities.

To be replaced by proposed new text:

(f) Category 6 - Special Purpose Entities –

(i) Special Purpose Insurers as defined under the Insurance Business (Special Purpose Insurer) Rules 2016; or

(ii) entities that the Commission agrees in writing may fall into this category.

This category is primarily intended for insurer's whose underwriting and counterparty credit risk are effectively eliminated - examples of these would include transformer cells, fully collateralised catastrophe cells, ILS cells and fully funded entities.



Guernsey Financial
Services Commission

INSURANCE BUSINESS (BAILIWICK OF GUERNSEY) LAW, 2002
FEEDBACK ON THE CONSULTATION PAPER ON RULES FOR
SPECIAL PURPOSE INSURERS

December 2016

This feedback paper reports on input received by the Guernsey Financial Services Commission on the Consultation Paper issued in October 2016 and consequent related changes.

Further enquiries regarding this feedback paper may be directed to:

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During October and November 2016 the Commission consulted on proposals to amend the framework underlying the Insurance Business (Bailiwick of Guernsey) Law 2002 (the “Law”) with the making of rules for Special Purpose Insurers and a related, minor amendment to the Insurance Business (Solvency) Rules 2015.

In making these proposals the Commission was responding to requests from industry, who believe that distinct rules for Special Purpose Insurers (“SPIs”) will assist in attracting Insurance Linked Securities business such as collateralised catastrophe reinsurance to the Bailiwick.

Feedback received and proposed changes

The Commission received a very small number of responses to this consultation, most of which referred to relatively minor points of drafting. Where appropriate the final Rules have been amended to reflect these comments. A number of substantive comments were received and these are addressed below along with the Commission’s response.

- A respondent asked why the definition of SPI refers only to cells of Protected Cell Companies and not to Incorporated Cells. It should be noted that Incorporated Cells would fall within the meaning of the term “insurer” which is also used in the definition of SPI.
- A respondent suggested that the subordination requirement for SPI capital be clarified. The Rules have been amended to clarify that subordination is to the claims against the assets of an insurer/cell and that subordination may be to a wider class of person than the insured. This comment has been accepted and the definition has been amended accordingly.
- A respondent suggested that the definition of Qualifying Investor used in the Rules should mirror the definition used in the Commission’s Qualifying Investor Fund Guidance (“QIF Guidance”). Consideration was given to this suggestion but the Commission’s view is that while this definition is appropriate for the QIF guidance, it is too broad a definition to be used in limiting investment in SPIs to parties with sufficient knowledge and resources to understand and participate in the alternative reinsurance market.
- A respondent commented that the proposed definition of Fully Funded Insurer, which permits the use of contingent capital where the capital provider is at a minimum rated A-, was too restrictive on the basis that providers of capital in such structures, though financially strong, are generally not rated. The Commission intends to give proper consideration to the widening of this restriction and assess the associated risks. The Commission does not intend to delay the issuance of the Rules while this matter is considered and, therefore, the relevant provisions of the Rules remain as consulted upon. Once the Commission’s assessment is completed the Rules may be amended as appropriate. However, otherwise, the stated approach to contingent capital will be applied by the Commission.

The Commission is grateful to the respondents for taking the time to consider and comment on the proposals.

Next Steps

The final version of the Insurance Business (Special Purpose Insurer) Rules 2016 is provided in the Annex to this document. The Rules will come into effect on 1 January 2017. The Insurance Business (Solvency) Rules 2015 will also be amended at this date to change the definition of a Category 6 insurer to include an SPI.

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rating (counterparty, credit or financial strength as applicable) of at least A- as of the date of application and as determined by an Acceptable Rating Agency;

- iii) according to the terms of such financing mechanism, the claims of participants in any such mechanism against the assets of the insurer or the cell are subordinated to the claims of creditors under the contracts of insurance underwritten by the insurer or cell;
 - iv) the insurer or cell only enters into contracts or otherwise assumes obligations or contingent liabilities which are solely necessary for it to give effect to the purposes set out from time to time in its agreed business plan; and
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