

CP12/13***

Financial Services Authority

Transposition of Solvency II

Part 2

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The Financial Services Authority invites comments on this Consultation Paper. Comments should reach us by 11 October 2012.

Comments may be sent by electronic submission using the form on the FSA's website at: www.fsa.gov.uk/library/policy/cp/2012/12-13-response.shtml

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It is the FSA's policy to make all responses to formal consultation available for public inspection unless the respondent requests otherwise. A standard confidentiality statement in an email message will not be regarded as a request for non-disclosure.

A confidential response may be requested from us under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Tribunal.

Copies of this Consultation Paper are available to download from our website – www.fsa.gov.uk. Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

This Consultation Paper will be made available in Welsh, upon request.

Abbreviations used in this paper

APR	Approved Persons Regime
BCRR	Base Capital Resource Requirements
BTS	Binding Technical Standards
CBA	Cost Benefit Analysis
CF	Controlled Function
CFPPFM	Consumer Friendly Principles and Practices of Financial Management
COBS	Conduct of Business Sourcebook
COLL	Collective Investment Schemes Sourcebook
CP	Consultation Paper
CP1	First consultation paper on transposition of Solvency II
CP2	This CP – the second consultation paper on transposition of Solvency II
CRR	Capital Resource Requirement
DB	Defined Benefit
DIA	Diversity Impact Assessment
EBA	European Banking Authority
ECR	Enhanced Capital Requirement
EEA	European Economic Area

EIOPA	European Insurance and Occupational Pensions Authority
EMIR	European Market Infrastructure Regulation
EPM	Efficient Portfolio Management
ESFS	European System of Financial Supervision
ESMA	European Securities and Market Authority
EU	European Union
FCA	Financial Conduct Authority
FICOD	Financial Conglomerates Directive
FIT	Fit and Proper Test for Approved Persons Sourcebook
FSMA	Financial Services and Markets Act 2000
GENPRU	General Prudential Sourcebook
GI	General Insurance
ICA	Individual Capital Assessment
ICG	Individual Capital Guidance
ICOBS	Insurance: Conduct of Business Sourcebook
INSPRU	Prudential Sourcebook for Insurers
IPRU(FSOC)	Interim Prudential Sourcebook for Friendly Societies
IPRU(INS)	Interim Prudential Sourcebook for Insurers
ISPV	Insurance Special Purpose Vehicle
ITS	Implementing Technical Standards
MCR	Minimum Capital Requirement
MoU	Memorandum of Understanding
NDF	Non-Directive Firms
ORSA	Own Risk and Solvency Assessment
OTC	Over the Counter
PPFM	Principles and Practices of Financial Management
PRA	Prudential Regulation Authority
RITC	Reinsurance to Close

RoIR	Reduction in Investment Risk
ROR	Reduction of Risk
RTS	Regulatory Technical Standards
SCR	Solvency Capital Requirement
SFCR	Solvency and Financial Condition Report
SOLPRU	Prudential sourcebook for Solvency II Insurers
SUP	Supervision Sourcebook
SYSC	Senior Management, Systems and Controls Sourcebook
USP	Undertaking Specific Parameters
UCITS	Undertakings for Collective Investment in Transferable Securities
UKLA	UK Listing Authority

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Overview

Introduction

- 1.1 This CP (CP2) is the second of the planned FSA consultations on rules to transpose the Solvency II Level 1 Directive (the Directive) in the FSA Handbook. This consultation programme is running in tandem with the Treasury's transposition of Solvency II, through amendments to the current Financial Services Bill, to implement the Directive.
- 1.2 Despite the ongoing uncertainties in the European timetable for finalising the requirements of Solvency II, we intend to have as many of the new rules as possible in place on the Solvency II transposition date. We expect to need to conduct further consultation to capture any remaining Handbook rules that correspond to those elements of Solvency II that are still evolving and so cannot be addressed earlier.
- 1.3 Our aim remains to clarify our proposed rules for Solvency II as early as possible where we have sufficient certainty. CP11/22 in November 2011 at: www.fsa.gov.uk/static/pubs/cp/cp11_22.pdf focused on the Level 1 requirements set out in the Directive. This CP picks up some of the topics held over from CP11/22, including areas where we have national discretion and rules specific to the UK insurance sector – in particular, Lloyd's market and with-profits business.
- 1.4 We have maintained the intelligent copy-out spirit of CP11/22, following the Level 1 text as closely as possible. In line with the mainly maximum harmonising nature of much of the Level 1 text of Solvency II, when drafting our proposed rules we have sought not to reopen discussions on policy that has been agreed in Europe. However, where the Directive points to areas of Member State discretion, we have responded to these in our draft rules and flagged the issues in our consultations.
- 1.5 Further background on our approach to consultation and an overview of the Solvency II framework can be found in CP11/22. In addition, up-to-date information on the current developments in Solvency II can be accessed at: www.fsa.gov.uk/about/what/international/solvency. Readers may also be interested in the Treasury's consultation document on

Solvency II, published in November 2011 www.hm-treasury.gov.uk/d/condoc_consultation_solvencyII.pdf.

Structure of the CP

- 1.6 Section I sets out how the Directive aligns with the on-going European legislative process and the programme of regulatory reform in the UK.
- 1.7 Section II contains feedback from stakeholders on CP11/22, in response to specific questions on transposing the prudential aspects of Solvency II. We have addressed and commented on some of the main points raised in stakeholders' feedback and have re-considered our approach in certain policy areas.
- 1.8 Section III sets out some new rules and guidance to form part of SOLPRU – the new prudential sourcebook for Solvency II insurers. The proposed rules and guidance address areas that were not covered, or were only partially covered, in CP11/22.
- 1.9 Both of the chapters in this section refer to the Directive articles, as appropriate, and to our overarching policy intentions. On Lloyd's market, we intend the rules to be woven into each chapter of SOLPRU, with the addition of a new application chapter at the end of SOLPRU.
- 1.10 Section IV proposes amendments to rules and guidance relating to other sourcebooks within the Handbook. The first two chapters relate to with-profits and unit-linked products where we intend to make respective changes to other sourcebook requirements, primarily COBS, in light of the Solvency II Directive. These changes will take effect at the same time as Solvency II is implemented, unless otherwise indicated. On with-profits, the rule changes aim to distinguish between Solvency II firms and out of scope Solvency II firms. It is important to note that none of the proposed changes impact on out of scope or otherwise non-directive firms (NDFs) firms, which will be subject to existing Handbook provisions.
- 1.11 The third chapter in this section deals with application rules (originally earmarked in CP11/22) and further consequential amendments to the sourcebooks. These, in the main, switch off and disapply provisions for Solvency II insurers in light of the new SOLPRU sourcebook. While most of these changes are minor and technical in nature, we draw particular attention to those with wider implications – and in a couple of instances to out of scope Solvency II firms.
- 1.12 In Sections III and IV, the relevant chapters also contain cost benefit analysis of the proposed changes in question, unless of minimal significance, in accordance with our responsibilities under sections 155 and 157 of the Financial Services and Markets Act 2000 (FSMA). This should be read in conjunction with the main CBA text set out in section IV of CP11/22.

- 1.13** The draft rules and changes to the Handbook (including SOLPRU) as a result of the proposals are set out in the Appendices.
- 1.14** The evolving European regulatory landscape may result in a few outstanding areas to be addressed in further consultation in due course. Outstanding issues may include aspects of Solvency II dependent either on the outcome of the Omnibus II Directive and Level 2 Solvency II measures or on EIOPA's formulation of guidelines as a Level 3 initiative. Known areas of these include the impact of transitionals on Solvency II, third country equivalence and the regulatory approach to third country branches.
- 1.15** A number of issues were also identified in CP11/22 for prospective inclusion in this CP. However, for various reasons, including delays in the European process for agreeing the Omnibus II Directive and ongoing developments in respect of UK regulatory reform, it has not been possible to address all of the outstanding issues in this CP.
- 1.16** The issues not covered, and reasons why, are:
- National Specific Reporting Templates – work on which has been integrated within an overall review of reporting and notification requirements under the jurisdiction of the PRA and FCA.
 - External audit – on which discussions are still ongoing within EIOPA and on which level 3 guidance is still being developed.
 - Further amendments to FIT and SUP to reflect changes in controlled functions – given that EIOPA guidance on the fit and proper assessment has yet to be finalised, and the need to understand the changes required to divide the approved persons regime between the PRA and FCA before we can confirm the final detail of any changes arising from Solvency II. In this light, we have now decided *not* to implement separate CF14 (risk function) and CF15 (internal audit) for Solvency II firms, as indicated in CP11/22, but to continue to regulate these functions under the existing CF28 function for the time being.
 - Grandfathering existing Insurance Special Purpose Vehicles (ISPVs) – as the need for transitional arrangements is influenced by the outcome of the level 2 legislation in respect of the provisions for ISPVs.
 - Cost comparisons of using internal models v Standard Formula for calculating firms' SCRs – as this is dependent on the availability of reliable and good quality data.
- 1.17** We intend to communicate further on these issues as and when appropriate.
- 1.18** In addition, at the time of going to print, we are communicating with insurance firms about the review and ongoing monitoring of internal models.

Scope

- 1.19** As noted in CP11/22, Solvency II will apply to about 550 firms, both retail and wholesale insurance firms, and be subject to SOLPRU. There also remain about 130 small firms, classified as non-directive firms (NDFs) under both Solvency I and II, the regulation of which will continue to conform to the existing Handbook rules rather than SOLPRU.
- 1.20** Similarly, firms that are out of scope of Solvency II, but subject to Solvency I, will come within the scope of existing Handbook rules, including IPRU (FSOC) for friendly societies and INSPRU, IPRU(INS) and GENPRU in the case of other insurance firms.
- 1.21** As we indicated in CP11/22, the specific rules and guidance applying to NDFs and other out of scope firms will be reviewed after Solvency II is implemented.
- 1.22** The mechanics for firms wishing to opt in to Solvency II, either of NDF or otherwise out of scope status, provided for under Article 4, will be finalised in further consultation.

Next steps

- 1.23** Responses to this Consultation Paper are due by **11 October 2012**. We will publish our response to feedback together with final rules relating to both this CP and CP11/22.
- 1.24** Readers are encouraged to refer to the Solvency II pages on the FSA website to keep pace with European and domestic developments on both policy and implementation.

Who should read this CP?

- 1.25** This paper will be of direct and primary interest to all insurance firms within the scope of Solvency II. It will also be of some interest to non-directive firms, and otherwise out of scope Solvency II firms, and of indirect interest to investment firms, representative trade bodies, business and financial advisers, and consultants.

CONSUMERS

The primary objective of the Solvency II Directive is to achieve an appropriate level of policyholder protection. Therefore, retail and commercial insurance policyholders may wish to take note of the general content of this paper.

Key messages for this CP

An on-going consultation process

Consultation timeline

We are continuing our consultation process to provide firms with the earliest possible certainty on the implementation of Solvency II in the UK. This consultation focuses on additional areas requiring transposition that remain outstanding from our first round of consultation, together with some areas where we have national discretion.

Further consultation

We will consult again as needed when the relevant aspects of the evolving European and UK regulatory landscape are sufficiently settled.

Limited scope for discretion

Intelligent copy-out

We continue to take a largely intelligent copy-out approach to transposition, following the Level 1 text as closely as possible.

Maximum harmonisation

This consultation reflects the mainly maximum harmonising nature of the Directive, and does not reopen discussions on policy (as set out in the Directive and reflected in our proposed rules) that has been agreed in Europe.

Where we have discretion

Where the Directive requires or permits Member State discretion, and where Handbook rules are needed to address national specificities, we invite comment on our policy decisions, as explained in the CP and reflected in our proposed draft rules.

Section I

Consultation process

Contents

2. European process
 3. Alignment with regulatory reform
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European process

Understanding the legal framework of Solvency II

- 2.1 Solvency II is being developed in accordance with the Lamfalussy approach, and is being amended by the Omnibus II Directive. The Omnibus II Directive is intended to bring Solvency II into line with the Treaty of Lisbon and the new European System of Financial Supervision (ESFS).

Levels of EU legislation under the Treaty of Lisbon

Level 1 (Legislative Acts)	<p>Framework legislation setting out the basic principles is proposed by the Commission and adopted by the European Council and European Parliament. The Solvency II Directive was agreed by the European Parliament and European Council in April 2009 and was published in the Official Journal in December 2009. The Omnibus II Directive will, through amendments to the Solvency II Directive, specify the scope of the delegation of power to the Commission to adopt Level 2 measures.</p>
Level 2 (Non-legislative Acts)	<p>These are developed by the Commission on the advice of EIOPA, and set out measures of application of the Level 1 text. As with Level 2 previously, the European Parliament has the power, by simple majority, to prevent adoption of the package as a whole, while the European Council may do so if it can achieve a qualified blocking majority of votes.</p>
Level 2 Binding Technical Standards (BTS)	<p>The Level 1 text may delegate to the Commission the power to adopt delegated acts or implementing acts that have been drafted by EIOPA. These are termed 'regulatory technical standards' (RTS) (if the delegations are made under Article 290) and 'implementing technical standards' (ITS) (if the delegations are made under Article 291). These standards 'should be technical, shall not imply strategic decisions or policy choices and their content shall be delimited by the legislative acts on which they are based'. After the Commission proposes RTS to the European Parliament and the Council, these two bodies may object to the RTS for up to three months. This three-month period is extendable by a further three months at the initiative of the European Parliament or Council. For ITS there is no further scrutiny by the European Parliament or the Council once they are adopted by the Commission for four years.</p>

Level 3	Guidance that is to be treated on a comply-or-explain basis by national supervisory authorities. Guidance is developed and adopted by EIOPA.
Level 4	The Commission, as the guardian of the Treaties, is responsible for ensuring that Directives are properly transposed and that EU legal requirements are then applied, pursuing enforcement action where required. Without prejudice to the Commission's powers, the EIOPA regulation envisages that EIOPA may play a role in investigating alleged breaches of EU law and following up actions.

State of play

- 2.3 At the time of publication, Omnibus II draft proposals are being discussed. Adoption and agreement on the Omnibus II Directive are necessary for the adoption process of the Level 2 text to start.
- 2.4 It is anticipated that the Level 2 text will be EU regulation and, as such, will apply directly to firms and supervisory authorities without requiring transposition into domestic law. Level 2 (as regulation) is therefore not subject to FSA consultation. This will also be the case for binding technical standards drafted by EIOPA (whether these are RTS or ITS), as these will similarly take the form of EU regulation. We expect EIOPA to consult on most Level 3 guidelines once Level 2 has been formally proposed by the Commission.
- 2.5 The draft Handbook text included in this CP is based on current text of the Directive and other European material formally available.

Why are we choosing to consult now?

- 2.6 Omnibus II is intended to introduce targeted changes to Solvency II. Amendments to the Directive that are expected to be introduced by Omnibus II will mainly cover:
- the introduction of technical standards and binding mediation mechanisms as set out in the EIOPA regulation; and
 - adjustments to the original Level 2 empowerments.
- 2.7 Omnibus II is also expected to introduce transitional provisions to ensure a smooth transition to the new regime.
- 2.8 Most of the policy set out in the Directive is stable and Omnibus II is not expected to affect the core principles of the Solvency II framework, as agreed when the Directive was adopted in 2009, which gives us sufficient certainty on much of the Level 1 text that must be transposed into the Handbook. If any changes arising out of the final text of Omnibus II are required, we expect to address these in further consultation.

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Alignment with regulatory reform

- 3.1** Over a similar timescale to the introduction of Solvency II, changes to the UK regulatory structure will split the FSA's powers and functions between two new regulatory bodies, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA). As the prudential regulator for insurance companies, the PRA will be responsible for most of the rules introduced by Solvency II, though the FCA will also have an interest through its own statutory objectives (for example, where Solvency II has implications for conduct of business) and responsibility for some rules relating to Solvency II. Regulatory reform will involve a range of changes to the current FSA Handbook of rules and guidance.
- 3.2** The provisional date by which both new bodies will be established depends on the timetable for passage of the Financial Services Bill through Parliament. Under current timescales, by the time of Solvency II implementation, the PRA will be responsible for the prudential regulation of all Solvency II firms (with the FCA interest as indicated above). The future operation of the rules by the PRA and FCA will be within the framework established by the new UK legislation and the Memorandum of Understanding (MoU) to be agreed between the PRA and FCA.
- 3.3** If, in the event, Solvency II is implemented before the PRA and FCA come into effect the rules text will be amended to reflect the single regulator with no further consultation.

Section II

Feedback on CP11/22 – Transposition of Solvency II – Part 1

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Feedback on CP11/22 – Transposition of Solvency II – Part 1

- 4.1** We received responses to *Transposition of Solvency II – Part 1* from 23 industry firms and organisations. A few responses were single-item comments only, but most related to a variety of topics and questions posed in the CP, varying in their length and complexity. The key points raised are summarised below, grouped according to the particular questions we posed in CP11/22.
- 4.2** We have amended some of the rules proposed in CP11/22 in response to feedback. The proposed revisions are included in Appendix 1. However, the rules will not be formally made at this stage.

Chapters 3 & 4 – General approach

Q1: *We welcome views on our approach to the overall consultation process proposed to transpose Solvency II: a first consultation (CP1) on the Directive requirements that have most certainty at this stage in the European process, followed by a second consultation in 2012 (CP2) once there is more certainty on Omnibus II, Levels 2 and 3, and the UK legislation has been finalised.*

Q2: *Do you have views regarding the clarity of our rules included in CP1, bearing in mind the limited scope for discretion?*

- 4.3 Most respondents were broadly supportive of our approach to transposing the Directive and recognised the implications of the continuing European uncertainties over the finalisation of the Omnibus II Directive and Level 2 measures. Most specific comment focused on areas where we had discretion to apply, or not to apply, certain Articles.

Chapter 7 – The Solvency Capital Requirement (SOLPRU4)

Q3: Do you agree with our approach to the Member State option outlined in Article 304?

- 4.4 This option relates to the duration-based equity risk sub-module for the SCR. A few respondents felt that the UK should apply this option on the grounds that it may at some time in the future benefit the industry, particularly for diverse pension provision. We have reviewed our position but do not believe it appropriate for the industry to adopt this module for the reasons set out in CP11/22.

Chapter 8 – The Minimum Capital Requirement (SOLPRU5)

Q4: Do you agree that we should exercise the case-by-case option in Article 129(3), for example when the internal model result has temporarily deviated from the risk profile for the firm and the standard formula is a better fit? Do you have views on any other situations where it would be appropriate to use this option?

- 4.5 Respondents supported the case-by-case approach to situations where the internal model deviates from the firm's risk profile, providing it was tempered with discretion. No suggestions were forthcoming of where such an option might be used in other situations.

Chapter 11 – Composites (SOLPRU8)

Q5: Do you agree with the approach suggested in this Chapter in relation to separate management of life and non-life business for composite firms?

Q6: Do you have any further comments on our proposals for the Handbook rules relating to composite firms?

- 4.6 There were no objections to the basic approach, but some respondents commented on the impact of the proposed rules for composites with long-term funds and how in particular these would be treated in relation to with-profits business, shareholder funds and winding-up provisions.
- 4.7 As a general response, with the disappearance of the concept of the long-term fund under Solvency II, we do not intend to provide any further rules or guidance on the separation of funds beyond those contained in SOLPRU 8. However, for with-profits and any other business that might fall within a ring-fenced structure, firms will need to await the final Level 2 and Level 3 measures to ascertain the detailed impact of ring-fenced funds on the overall business.
- 4.8 Further, the Directive does not envisage a shareholder fund, as a non-attributed fund, being created. Instead, any assets previously held in such accounts should be re-allocated either to the life or non-life business accordingly. Similarly, the current winding-up rules do not generally set any different level of preference for creditors for life and non-life business in relation to the assets of the company, irrespective of whether these are designated before insolvency as being attributed either to life or to non-life business.

Chapter 12 – Conditions governing business (SOLPRU 9)

Q7: Do you consider that the Approved Persons Regime (APR) is the appropriate method for us to implement the Article 42 requirements regarding receiving notifications and making assessments on personnel?

- 4.9 Firms' responses did not raise any significantly new issues that would suggest a need to re-consult or reassess our approach.

Q8: Do you agree with our approach to assessing third party providers where a key function has been outsourced?

- 4.10 Several respondents raised concerns over the need to apply 'fit and proper' requirements on a selective basis to outsourcers and felt that it should be applied on a proportionate basis or only in the most exceptional circumstances.
- 4.11 The approach we proposed in CP11/22 to assessing third-party providers where a key function has been outsourced is primarily concerned with ensuring that we are compliant with Solvency II, while also able to obtain the necessary assurance that individuals working within a key function in a third party service provider meet fit and proper requirements in respect of their roles.

- 4.12** Under Solvency II, firms will be required to assess the fitness and propriety of the individuals in the third-party provider working in an outsourced key function. Given our reliance on these assessments, in the interests of protecting policyholders, we will review a firm's assessments and/or conduct an additional fit and proper assessment of the individuals in the third-party provider responsible for the outsourced function. While we do not envisage these reviews being frequent, we will determine their need on the basis of our risk-based supervisory methods and criteria.

Chapter 14 – Groups (SOLPRU11)

Q9: Do you agree with the way we are proposing to exercise the Member State option in Article 227?

- 4.13** There was broad support for allowing the use of local rules under Article 227.

Q10: Do you agree with the way we are proposing to exercise the Member State option in Article 225?

- 4.14** Under Article 225 of Solvency II, Member States have the discretion to decide, for groups that include an insurance firm based in another Member State, whether to allow the group solvency calculation to take account of the SCR and own funds requirements as laid down in that other Member State for the firm's contribution to the group solvency position.
- 4.15** Responses were broadly supportive, but some concern was expressed over how the option would work in practice, such as its interaction with the other group solvency calculation rules, and the approval process for allowing the use of other Member States' application of the solvency requirements.
- 4.16** The option under Article 225 will be exercised by allowing the use of the requirements applied in the EEA Member State as a general rule, without needing further approval. However, we will keep in view any significant changes to the solvency regime of the relevant Member State and may reconsider the use of the Member State calculation in those circumstances. The option will apply under both calculation methods (accounting consolidation and deduction and aggregation), where the calculation allows for it.
- 4.17** The group supervisor will be able to discuss the use of the option under Article 225 with the relevant supervisory authorities in the college.

Chapter 16 – SUP 10

Q11: Do you agree with our proposed approach to those currently approved for CF28 because of their finance responsibilities? Or do you think one of the alternative options discussed above would be preferable?

- 4.18** This question yielded significant feedback, with firms indicating different preferences for the options provided on the grounds that their preferred alternative would represent a simpler and more permanent solution, with less administrative burden.
- 4.19** We are conscious that further changes may need to be made to the approved persons regime as a result of regulatory reform. With this background uncertainty, we would like to minimise any potential burden that might arise for Solvency II firms from having to reassign individuals currently within the CF28 designation.
- 4.20** We have therefore decided to amend our original proposal to introduce separate controlled functions for risk and audit as part of Solvency II implementation, and will instead continue to regulate these functions under the existing CF28 function. We expect that the introduction of specific controlled functions for risk, audit and finance will form part of the PRA/FCA regime at some point in the future. So any changes will be made as part of the broader regulatory reform programme rather than as part of Solvency II implementation. More information will be provided during a further consultation we expect to undertake later this year, which will propose and explain how the Approved Persons Regime will work for the PRA and FCA.
- 4.21** For Solvency II firms, we intend that individuals currently approved within CF28 for risk, internal audit and finance roles will retain CF28 until the other changes related to regulatory reform come into effect. These changes may occur before or after implementation of the Directive. To comply with Solvency II requirements, firms will be asked to notify the FSA regarding which of the specific risk, internal audit and finance roles individuals currently within CF28 will be fulfilling.

Annex 1: Diversity Impact Assessment

Q12: Do stakeholders agree with our findings from this Diversity Impact Assessment?

- 4.22** We received limited feedback from stakeholders on the Diversity Impact Assessment (DIA) opining that, ultimately, certain groups of people, whether designated as statutory or otherwise under equality law, may be at greater risk as a consequence of firms re-shaping their business strategy in response to having to meet new capital requirements. We have

considered this possibility but we do not believe that there is any direct correlation between the Directive and equality provisions on the grounds that:

- a) individual business decisions of this nature are unlikely to be solely motivated by capital considerations but rather a mix of inter-related factors;
- b) it is difficult to comprehend circumstances where decisions of this nature will lead to certain groups of policyholders being excluded from obtaining insurance protection universally; and
- c) insurance provision will remain a competitive industry and consumers will be able to exercise freedom of market choice if they believe they are being ‘priced out’ of a particular product by the actions of an individual insurer.

Other feedback

- 4.23** We did not receive any significant challenge from stakeholders about our cost benefit analysis, although one respondent commented that the implementation burden would be more significant for small insurers due to in-house human resource constraints, with a disproportionate dependence on outsourcing. However, there was no specific cost data to support this assertion.
- 4.24** Finally, a few observers commented on outstanding issues such as supervision of third country branches and external audit, and queried when rules and guidance may be expected. In light of ongoing work within EIOPA and other parts of the evolving regulatory landscape, material is expected to be available on these and other topics in due course.

Section III

The new prudential sourcebook for insurers – SOLPRU

Contents

5. Our approach to the Lloyd's market
 6. Public disclosure of Capital add-ons and USPs
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5

Our approach to the Lloyd's market

Introduction

- 5.1 This chapter sets out how we propose in SOLPRU to apply the Solvency II requirements to the Lloyd's market (defined as 'the association of underwriters known as Lloyd's' in the Directive).
- 5.2 The Lloyd's market poses specific challenges in the context of implementing Solvency II due to its unique structure and its multiple participants which, for the purposes of this chapter, includes:
- Members (comprising both individual 'Names' and corporate members): these are capital providers for the Lloyd's marketplace, and are risk carriers by virtue of accepting the underwriting risks for insurance business written. Each member has several liability.
 - Syndicates: one or more members considered together for accounting purposes to carry out underwriting business for a year of account and for a specified class or classes of business. Members can belong to multiple syndicates, and syndicates are constituted on an annual basis.
 - Managing agents: undertake underwriting decisions on behalf of the members of a syndicate and manage the business written by syndicates – a managing agent can manage more than one syndicate.
 - The Society of Lloyd's oversees managing agents and syndicates. This includes monitoring the capital that members provide to support their underwriting, monitoring the performance of syndicates to improve performance and undertaking financial and regulatory reporting for the Lloyd's market.

- 5.3 Our proposed approach reflects the level at which we believe the requirements should be applied – managing agents, the Society, or a combination of both.
- 5.4 These rules have been formulated with two fundamental principles in mind:
- Policyholders with policies at Lloyd’s should benefit from the same threshold level of policyholder protection as other Solvency II policyholders do.
 - We should in general seek to apply the Directive requirements at the level where risk is managed.
- 5.5 We have sought to apply to Lloyd’s the SOLPRU rules and guidance set out in CP11/22 and have only developed specific, additional provisions where required and supplemented by a new application chapter, SOLPRU14.

Pillar 1 requirements

Articles 100 to 102 – Calculating the SCR (SOLPRU 4)

- 5.6 We propose that the SCR should be applied at the Society level to take account of:
- the risks arising from members carrying out underwriting activities in the Lloyd’s market, including risks relating to the assets and liabilities that represent members’ own funds at Lloyd’s; and
 - risks arising to the funds and property of the Society (including assets and liabilities available to meet the liabilities of members), more specifically:
 - risks that members will not hold sufficient capital either as to quality or amount, in respect of the risks to which they are exposed; and
 - any other risks (for example, operational risks associated with managing the funds and property of the Society).
- 5.7 We also propose to require managing agents to calculate a notional SCR for each syndicate they manage.

Articles 128 to 131 – Calculating the MCR (SOLPRU 5 & 8)

- 5.8 As the Directive requires separate notional MCRs for life and non-life business, we propose that the notional life and non-life MCR be calculated for the Lloyd’s market in its entirety, reflecting the composite nature of the market (as it consists of syndicates which separately write life and non-life business).

- 5.9 We also propose to require the calculation of a ‘reporting point’ for each member, calculated as X% of member notional SCR (where X is the ratio of Lloyd’s MCR to Lloyd’s SCR).

Proposed application for other Pillar 1 areas

Article 75 – Valuation of assets and liabilities (SOLPRU 2)

- 5.10 Valuation will be required for all levels of Lloyd’s where assets are held; managing agents will be required to undertake valuations for each syndicate they manage, and valuation will be done centrally for members and for the Society. This is necessary to cover the central assets and liabilities and where members belong to multiple syndicates.

Articles 76 to 86 – Technical provisions (SOLPRU 2)

- 5.11 Our policy on technical provisions will be to require managing agents to perform the calculations for each syndicate, in addition to a requirement for calculations at Society level.

Pillar 2 requirements

Articles 41 to 50 – Governance and risk management (SOLPRU 9)

- 5.12 For **governance and risk management**, our policy will be to apply the Directive requirements at both Society and managing agent level. This includes:
- Solvency II functions (risk management, internal audit, compliance and actuarial);
 - risk management and internal control systems;
 - fit and proper regime;
 - general governance; and
 - remuneration and outsourcing.
- 5.13 The overarching reason for extending these requirements to managing agents is that members’ insurance business is managed by managing agents.

Q1: Do you have any views on whether, and if so, how we should replace our existing requirement in respect of the provision of statements of actuarial opinion?

- 5.14 An **Own Risk and Solvency Assessment (ORSA)** will be required to be produced by managing agents for each syndicate they manage because of differing risk profiles. This is in addition to a requirement for a Society level ORSA.

Article 132 – Prudent Person Principle (SOLPRU 7)

- 5.15 In terms of the **Prudent Person Principle**, the requirements need to be applied at all levels where assets are managed or invested. So, we will require application of the principle at managing agent level, for each syndicate managed, and at Society level.

Article 210 – Finite reinsurance (SOLPRU 9)

- 5.16 For **Finite reinsurance**, our policy will be to apply the Directive at managing agent and Society level, as this will capture all relevant risk across the Lloyd's market.

Cost benefit analysis

Direct costs to the FSA

- 5.17 The draft rules for Lloyd's do not change our original assessment of direct costs presented in CP11/22.

Capital compliance costs

Pillar 1 requirements

SCR

- 5.18 In CP11/22 we included estimates of the industry's costs from raising and servicing capital to meet Solvency II rules, taking firms' capital under our ICAS regime as the baseline. This analysis included capital compliance costs for Lloyd's.
- 5.19 In order to apply the SCR requirements to Lloyd's, we are proposing a central requirement (an amount reflecting the loss in basic own funds at a 99.5% confidence level calculated for the central funds of the Society) but do not expect this to create incremental capital costs beyond those for meeting the SCR.

- 5.20 In practice, whether the Society of Lloyd's would incur incremental costs depends on two factors. First, commercial incentives mean Lloyd's may take action to ensure syndicates do not expose central assets to risk beyond the Society's appetite for it, with the effect of reducing the level of the central requirement and increasing eligible own funds held by members (the incremental costs of which are included in our estimates for meeting the SCR). Second, if the calibration of the SCR is such that Lloyd's simultaneously satisfies the SCR and the central requirement, then the Society would not need to raise capital.

MCR

- 5.21 We are proposing that Lloyd's calculate the MCR at the level of the market. This will not impose any incremental capital compliance costs because the combined effect of the MCR and requirements for eligible own funds is less than that of the Lloyd's SCR, i.e. if the SCR is met then the MCR will be met too, as is the case for other entities.
- 5.22 We are proposing that Lloyd's calculates 'reporting points' for members. If eligible own funds fall below these thresholds then the FSA may take supervisory action. Passing these thresholds does not, however, constitute a breach of the MCR. Incremental compliance costs arising from supervisory action will depend on whether these thresholds are breached, the type of supervisory response, and the cost that this imposes on members and the Society of Lloyd's, and cannot be predicted in advance.

Non-capital compliance costs

- 5.23 We included industry-wide estimates of the non-capital costs of complying with SOLPRU rules in CP11/22. Lloyd's have confirmed that relative to their estimates of their costs of complying with those rules, the rules we are proposing in this consultation do not add incremental costs.

Indirect costs

- 5.24 Our estimates of incremental compliance costs identified in this chapter are not sufficient to cause us to revise our conclusions on indirect costs presented in CP11/22.

Benefits

- 5.25 We presented our analysis of the overall benefits of Solvency II in CP11/22. Below we focus how our proposals for applying Solvency II to Lloyd's gives rise to benefits.
- 5.26 While it is possible to identify the individual components of incremental cost, it is not straightforward to do the same for benefits, since the effects of the proposed requirements interact with one another. For instance, Pillar 2 requirements reinforce Pillar 1

requirements in how risk is identified, managed and capital is provisioned. And Pillar 3 improves information to supervisors and the market, increasing transparency about both quantitative and qualitative information.

- 5.27** We discussed in CP11/22 that we expect the main benefits of Solvency II to UK policyholders to arise from improved risk management and governance, resulting in an improved ability of insurers to meet contractual obligations. We reach the same conclusion for Lloyd's policyholders.
- 5.28** While we expect neither the central requirement nor the reporting points to have a material incremental effect on capital held, we do expect them to strengthen Lloyd's incentives to ensure risks within the market are managed to ensure at least the same standard of policyholder protection as for other Solvency II policyholders. In addition, we expect, the central requirement and reporting points to aid our supervisory intervention by identifying clear thresholds for capital held in respect of risks arising to member and central assets and liabilities, within the overall structure of Society-level capital requirements.
- 5.29** We expect aligning Pillar 2 requirements to the level at which risk is managed to improve decision-making and control about risks carried.

Summary

- 5.30** Our proposals should not add materially to the costs already considered in CP11/22. We expect them, however, to ensure that the protection available for policyholders of Lloyd's meets the same standards as those for policyholders of other insurance entities.

6

Public disclosure of Capital add-ons and USPs

Introduction

- 6.1** Under Article 51(2) of the Directive, Member States have the option to activate a transitional provision during a specified period up to and expiring on 31 October 2017. During this time firms would not have to: 1) separately identify or disclose any capital add-ons nor the justification given by the supervisory authority for their imposition; and/or 2) disclose the impact of any undertaking specific parameters (USPs) nor the justification given by the supervisory authority for their imposition, when their use was required by the supervisor under Article 110.
- 6.2** The default requirement under the Directive is for public disclosure of any capital add-on and USP as part of the annual Solvency and Financial Condition Report (SFCR). The material below builds on our consideration in CP11/22 (SOLPRU 12.3.5) of the option provided in Article 51(2).
- 6.3** As a formal requirement, the SFCR has to include the amount of the firm's Solvency Capital Requirement (SCR) and Minimum Capital Requirement (MCR), showing separately (if relevant):
- a) SCR calculated using the standard formula;
 - b) SCR calculated using an internal model;
 - c) amount of any capital add-on imposed in accordance with Article 37 of the Directive; and
 - d) impact of any USP the firm is required to use in calculating the SCR using the standard formula in accordance with Article 110 of the Directive.

- 6.4 In the case of the information in c) and d), this should include concise information on the justification given by the supervisory authority for requiring the USP or imposition of the capital add-on.

Proposal

- 6.5 We now intend to exercise the option of non-separate disclosure of any capital add-ons or the required use of USPs as contemplated in Article 51(2) by providing firms with a transitional period of non-disclosure that would cover the first *two years* following the Solvency II implementation date.
- 6.6 During this transitional period, firms would not need to separately disclose in their SFCR any capital add-ons or USPs required by a supervisor under Article 110. On the present implementation timetable, this means that the transitional period will apply to disclosures of SFCR made for the first two financial years following the Solvency II implementation date.
- 6.7 It should be noted that this proposed transitional will not affect the requirement by which firms need to disclose their total SCR within the SFCR, and to include within it any capital or USP (even though it is not *separately* disclosed).
- 6.8 For the sake of clarity, it should also be noted that this proposal relates solely to prudential reporting requirements and not to the Listing Rules or the Disclosure Rules and Transparency Rules maintained by UKLA which were the subject of an earlier CP in 2012 (CP02/12).

Cost benefit analysis

- 6.9 In summary, we consider market disclosure to be valuable, but during the transitional period there is potential for disclosure to have unintended consequences as the market adapts to the new system under Solvency II. Therefore, we expect the costs of non-disclosure to be outweighed by the benefits.

Costs

- 6.10 We do not believe that the lack of disclosure of either capital add ons or USPs during the transitional period is likely to lead to substantial costs, particularly while firms and supervisors adjust to the new regime.
- 6.11 Although non-disclosure of capital add-ons reduces the amount of information available to market analysts during the transitional period, we do not think the costs from non-disclosure of a capital add-on for a deviation of the risk profile from the SCR calibration would be large. First, other sources of public information are available, such as Solvency and Financial

Condition Reports and financial statements. Secondly, the capital add-on could be a temporary measure while internal model approval is sought. Thirdly, the frequency of capital add-ons for a deviation in risk profile from the SCR calibration is likely to be higher in these first two years as firms adapt to the new regime than after the regime has been in place for several years, although we cannot be certain until the regime is implemented. This means that the information content of this disclosure is likely to be lower than once the regime has been in place for several years and firms have adapted to it. Where a capital add-on is due to inadequate governance the loss of market disclosure is a more significant cost because this information is not available from other sources and it could materially affect investor decision-making.

- 6.12** With regard to non-disclosure of USPs, similar arguments apply in respect of other sources of information being available and deviations in the risk profile. Similarly, a USP could (in some cases) be an interim measure as a firm works towards internal model approval, in which case its use would not necessarily be a reliable guide to future calibration of the SCR.

Benefits

- 6.13** We consider that not requiring firms to separately disclose capital add-ons or the required use of USPs during this initial two-year period would provide the market with a period of time during which it could develop a better understanding of add-ons and USPs. This would allow the market to transition from our current regulatory regime to Solvency II with less likelihood of overreaction when any implications of capital add-ons or USPs are not yet well understood across the market.

Q2: Do you agree with our approach to exercising this option?

Section IV

Amendments to other parts of the Handbook

Contents

7. With-profits insurance business
 8. Linked long-term insurance business – derivatives, stock lending and governance
 9. Consequential amendments to the Handbook
-

7

With-profits insurance business

Introduction

- 7.1 This chapter presents proposals for changes to our rules and guidance relating to the operation of with-profits insurance policies, as a consequence of Solvency II, primarily in the Conduct of Business Sourcebook (COBS) 20 *With-profits*. The proposed changes outlined in this chapter are intended to make consequential, and largely technical, changes to the current rules so that they are consistent with the requirements of the Directive. We are not making material changes to our underlying policy on conduct regulation for with-profits funds. These proposals do not conflict with recent changes made to COBS 20 which were implemented on 1 April 2012 as part of the ‘With-Profits Regime Review’, and any future changes will be consulted on separately.

The current rules

- 7.2 To understand how COBS 20 will need to be amended to achieve its aims under the Solvency II Directive, we summarise below its current structure and impact. It is divided into five sections:
- COBS 20.1 sets out the application of the rules. It states that the rules apply to life insurers that write with-profits business in the UK which includes domestic insurers and, under certain conditions, EEA insurers (when the matters has not been reserved to their home regulator).
 - COBS 20.2 includes sections covering:
 - payouts under contracts;

- distribution of excess surpluses;
 - charges taken from with-profits funds;
 - terms on which new business is written;
 - how relationships with connected persons should be treated;
 - provides guidance on investment strategies;
 - how major changes to funds should be managed and what must happen on closure to new business; and
 - reattributions of inherited estates.
- COBS 20.3 sets out the requirements for the production and contents of the Principles and Practices of Financial Management (PPFM).
 - COBS 20.4 describes the communications required from the firm to with-profits policyholders including production of a customer friendly PPFM and an annual report.
 - COBS 20.5 describes governance requirements and the responsibilities of with-profits committees.

7.3 In addition, some rules on the governance of with-profits business are currently elsewhere in the Handbook, including:

- INSPRU 1.1, which contains rules requiring insurers to ensure that they have sufficient assets in their with-profits funds to cover the liabilities of those funds.
- INSPRU 1.5 where there are several sections relevant to with-profits business such as ring fencing provisions in relation to long-term insurance funds and sub-funds, including restrictions on transfers out of such funds.
- GENPRU where rules and guidance for capital instruments for insurers carrying on with-profits business are contained in Chapter 2 (2.270-2.275), including key conditions that must be met before such instruments can be included in the firm's reported capital resources.
- IPRU (INS), which includes in Chapter 3 (3.2, 3.3 and 3.5) rules about dividend payments, allocation of surplus and fairness between funds.

7.4 It is proposed that most of these rules will be incorporated in some form into COBS 20 for Solvency II firms. Provisions that are moved from the current prudential sourcebooks to COBS will generally not be applied to incoming EEA firms except to the extent that they are considered not to fall within the responsibility of the home state.

Table showing location of current Handbook rules and their proposed new position in COBS 20 for Solvency II firms

Reference	Current rules	Proposed new position	Outcome
COBS 20.1.1R-20.1.5R	Application of COBS 20	COBS 20.1.1R-20.1.5R	Amended rule
N/A	Treating of other liabilities	COBS 20.1A.1AR	New rule
INSPRU 1.1.137R (2)	Treatment of planned enhancements	COBS 20.1A.1R (SOLPRU 2.4.24G)	New rule and guidance
INSPRU 1.5.22R(2) and 1.5.25G	Rules and guidance on the identification of sub-funds	COBS 20.1A.2R & 20.1A.3G	New rules and guidance
INSPRU 1.5.23R & 1.5.24G	Rules and guidance on the requirements to separately identify assets relating to with-profits business and for separate accounting records to be maintained	COBS 20.1A.4R & 20.1A.6R & 20.1A.7G	Replacement and amended rule and guidance
INSPRU 1.1.27R & 1.1.28R	Requirement to hold sufficient assets to meet liabilities	COBS 20.1A.5R	Replacement and amended rule and guidance
INSPRU 1.5.27R & 1.5.28G	Transfers of assets from with-profits funds	COBS 20.1A.8R & 20.1A.9G	Replacement and amended rule and guidance
INSPRU 1.5.30R-1.5.32G	Rules and guidance on exclusive use of assets	COBS 20.1A.10R-20.1A.12G	Replacement and amended rule and guidance Consequential changes to INSPRU
GENPRU 2.2.271R	Capital instruments	COBS 20.1A.14R-20.1A.15G	New rules/guidance
IPRU(INS) 3.5R	Avoiding unfairness between separate funds	COBS 20.1A.16R	Replacement rule
COBS 20.2.1G-20.2.2R	Introduction to treating with-profits policyholders fairly	COBS 20.2.1G-20.2.2R	Unchanged provisions
COBS 20.2.3R-20.2.16R	Amounts payable under with-profits policies	COBS 20.2.3R-20.2.16R	Unchanged provisions
N/A	Guidance on distributions	COBS 20.2.16BG-20.2.16CG	New guidance
COBS 20.2.17R-20.2.20R	Conditions relevant to distributions	COBS 20.2.17R-20.2.20R	Amended rule (2.17 and 2.18)

IPRU(INS) 3.3R	Changes in the proportion distributed to policyholders	COBS 20.2.19AR-20.2.19CG	Replacement and amended rule and guidance
COBS 20.2.21R-20.2.22E	Requirements relating to the distribution of excess surplus	COBS 20.2.21R-20.2.22E	Amended underlying definition excess surplus
COBS 20.2.23R-20.2.27R	Charges to a with-profits fund	COBS 20.2.23R-20.2.27R	Unchanged provisions (consequential change to COBS 20.2.25R)
INSPRU 1.5.33R	Financial penalties levied by the FSA	COBS 20.2.26AR	Replacement rule
COBS 20.2.28R-20.2.31G	New business	COBS 20.2.28R-20.2.31G	Unchanged provisions
COBS 20.2.32R	Relationship of the with-profits fund with the firm and any connected persons	COBS 20.2.32R-20.2.32BG	Disapplied rule but new guidance
COBS 20.2.33G-20.2.34G	Contingent loans and other forms of support for the with-profits fund	COBS 20.2.33G-20.2.34G	Amended guidance
N/A	Rule on disclosure of support arrangements	COBS 20.2.34AR	New rule
COBS 20.2.35G-20.2.38G	Other rules and guidance on the conduct of with-profits business including rule on strategic investments	COBS 20.2.35G-20.2.38G	Disapplied most existing rules and guidance. New guidance
COBS 20.2.39R-20.2.52G	Major changes in with-profits funds including the process for reattributions	COBS 20.2.39R-20.2.52G	Unchanged provisions
COBS 20.2.53R-20.2.60G SUP App 2.15	Ceasing to effect new contracts of insurance in a with-profits fund	COBS 20.2.53R-20.2.60G	Unchanged provisions Consequential amendments to SUP App 2.15
COBS 20.3.5R	Scope of principles and practices of financial management	COBS 20.3.5R	Amended rule
COBS 20.4.4R	Communication with with-profits policy holders: requirements on EEA insurers	COBS 20.4.4R	Amended rule

COBS 20.5.3R	Governance and responsibilities for with-profits committees	COBS 20.5.3R	Amended rule
N/A	Transitional arrangements for with-profits funds	COBS TP2.23R	New rule

- 7.5 There are also a number of definitions relating to with-profits business that are relevant to COBS 20 and other Handbook provisions set out above and which will need to be revised as proposed in this chapter. Reference to Solvency II firms in this chapter is generally a reference to Solvency II firms to whom SOLPRU applies but where the context permits may also refer to incoming EEA firms.

Proposed changes to COBS 20

COBS 20.1A The with-profits fund

- 7.6 This is a new section of COBS 20 in which we propose to import most of the various rules from other parts of the Handbook as set out in more detail below.

COBS 20.2 Treating with-profits policyholders fairly

Amounts payable under with-profits policies (COBS 20.2.3-16)

- 7.7 We do not consider that these rules are directly impacted by the Directive but they are affected by changes to the glossary definitions and cross references to new corresponding provisions in SOLPRU.

Conditions relevant to distributions (COBS 20.2.17-20)

- 7.8 The rules in this section are designed to reinforce the need for firms to manage their funds prudently. They achieve this by ensuring that the cost of any distribution can be met from the regulatory surplus within the fund. The definition of regulatory surplus is currently the excess, if any, of the regulatory value of the assets (as defined in INSPRU 1.3.24) in the with-profits fund over the regulatory value of the liabilities (in INSPRU 1.3.29).
- 7.9 We propose a new definition of with-profits fund surplus to replace regulatory surplus in COBS 20.2.17. This definition will capture the concept of surplus, which is broadly similar to the existing concept of surplus over the realistic value of liabilities, i.e. as the difference between:
- 1) the value of the assets of the with-profits fund identified in accordance with COBS 20; and

- 2) the value of the technical provisions for the policies written in (or transferred into) that with-profits fund and the value of the other liabilities in the fund.

Calculated in accordance with SOLPRU 2 and level 2 text and as determined by actuarial investigation.

- 7.10** However, it is important to note that the rules in COBS 20 on distributions will continue to apply to all distributions that Solvency II firms make. We are, therefore, adding guidance at COBS 20.2.16BG and 16CG so that distributions will mean any distribution of distributable profits, namely any permanent addition to policy benefits made at the firm's discretion based on the investment or other experience in the fund more generally. This would include distributions relating to expected payments that are expected to be affordable and for which allowance has already been included within the technical provisions. As such, these are not just distributions of 'surplus' which will become a narrower concept. Distributions will continue to include payments of cash bonus, terminal bonus on exit and a declaration of reversionary bonus. We also clarify in guidance that, in relation to distributions from excess surplus, distributions also includes amounts that are added to asset shares or to any other measure that is used to determine payouts under policies.
- 7.11** It is also important to note that the concept of the with-profits fund surplus in COBS rules will be slightly different from the concept of approved surplus funds for the purposes of SOLPRU (see SOLPRU 2.4.24G). We are introducing a rule to make clear that the with-profits fund surplus for COBS purposes is net of planned enhancements currently dealt with in INSPRU 1.3.137R(2), whereas such amounts potentially fall inside the concept of approved surplus funds. We propose to clarify in COBS 20.1A.1R(2) the treatment of the value of future transfers to shareholders. These will be reported to us on national specific templates, the detail and collection requirements for which will be the subject of consultation at a later date. We also propose to clarify in COBS 20.2.17R(1) (b) for Solvency II firms that we expect them to be able to afford any distribution that leads to planned enhancements to benefits.

Q3: Do you agree with the changes that we have described above to the conduct rules for distributions?

Requirements relating to distribution of an excess surplus (COBS 20.2.21-22)

- 7.12** The current rule requires firms to consider each year whether they have an excess surplus in a particular with-profits fund. An evidential provision then provides that if there is an excess surplus and that to retain it would be a breach of Principle 6, the firm should make a distribution from the relevant with-profits fund.
- 7.13** We propose that Solvency II firms should keep the concept of the excess surplus. We propose to achieve the same outcome by replacing the concept of the 'regulatory surplus'

and realistic value of assets over liabilities with that of the surplus of assets over technical provisions and other liabilities. The with-profits fund surplus will have to be distributed in due course if/when the fund declines and runs off. We also propose to make changes to the references to capital requirements to reflect requirements under the Directive.

Q4: Do you agree with our proposal to amend the definition of excess surplus for the purposes of the rule and evidential provision relating to the distribution of excess surplus?

Charges to a with-profit fund (COBS 20.2.23-27) and new business (COBS 20.2.28-31)

- 7.14** These sections of COBS 20 outline the way in which firms may charge costs and contributions to tax to with-profit funds, and the terms on which new business in a with-profit fund may be written.
- 7.15** We propose to introduce into the charges section of COBS 20 a provision for Solvency II firms with the same effect as the current rule INSPRU 1.5.33R about the allocation of financial penalties for non-mutual firms.

Connected persons (COBS 20.2.32)

- 7.16** This rule restricts the circumstances in which a firm may make loans or guarantees to connected persons using assets in the with-profits fund.
- 7.17** It appears to us that granting a loan using assets in the with-profits fund is likely to be regarded as an investment of those assets and therefore covered by Article 132 (the Prudent Person Principle). As such, we propose to disapply the rule for loans made by Solvency II firms.
- 7.18** We propose new guidance for Solvency II firms for loans made using assets in the fund. This is based on the current rule requirement in COBS 20.2.32(4) and sets out the FSA's expectation that any loans will be in the best interests of policyholders in the reasonable opinion of the firm's senior management. This is desirable for the continued protection of policyholders, and is supplementary to and consistent with the provisions implementing the Prudent Person Principle (which requires that, in cases of conflict, assets shall be invested in the best interests of all policyholders and beneficiaries).

Q5: Do you agree that for Solvency II firms we should disapply COBS 20.2.32R in relation to loans and produce new guidance as proposed?

Contingent loans and other support (COBS 20.2.33-34)

- 7.19** In retaining this guidance we propose amending the text to make clear that references to realistic reporting firms are not relevant to Solvency II firms. We shall also clarify our intention that this applies to assets held within the fund.
- 7.20** We also propose introducing a new rule for Solvency II firms, as COBS 20.2.34AR on support assets, requiring that the terms and conditions for assets outside a with-profit fund, including those regarding the circumstances in which repayment will be required, need to be adequately recorded and explained to policyholders, including in their PPFM. The current COBS 20.2.34G will continue to apply to all firms but we propose to amend it to make it clear that firms may only manage their with-profit funds taking into account support arrangements that have been formally approved.

Q6: Do you agree that we should retain the guidance as proposed, and introduce a new rule on support assets?

Other rules and guidance on the conduct of with-profits business (COBS 20.2.35-38)

- 7.21** The Prudent Person Principle will place requirements on firms' investment of assets on a firm-wide basis. Our expectation is that firms should take account of the particular liabilities within the with-profits fund when investing assets in their with profits funds. We propose to include new guidance for Solvency II firms about our expectations of how firms will apply the Prudent Person Principle in the context of their with-profits funds, including for strategic investments. We also propose to disapply current rules and guidance about investment strategy and strategic investments but retain other guidance about reviewing non-profit business, reinsurance and disclosure of decisions on strategic investments.

Q7: Do you agree to our retaining guidance on reviewing non-profit business, reinsurance and disclosure of decisions on strategic investments for all firms, but that for Solvency II firms that we disapply the rules and guidance referred to above which overlap the Prudent Person Principle?

Q8: Do you agree that we should introduce guidance to Solvency II firms writing with-profits business that the provisions implementing the Prudent Person Principle should be applied to the investment of with profits assets by reference to the particular circumstances within the with profits fund including in relation to strategic investments?

*Ceasing to effect new contracts of insurance and run-off plans
(COBS 20.2.53-60 and SUP Appendix 2.15)*

7.22 These rules require the firm to advise the FSA and policyholders if it has ceased to effect new contracts of insurance and to submit prescribed information to the FSA. We propose to change the details of the information required to be submitted (contained in SUP Appendix 2.15) only to the extent that we need to – primarily that for Solvency II firms the terminology will change for the balance sheet and financial projections that form part of the requirements (see Appendix 6 for details).

Q9: Do you agree that the changes to the provisions on ceasing to effect new business should be restricted to those required to align the rules with Solvency II terminology?

IPRU (INS) Chapter 3

Distributions

7.23 The rules in IPRU (INS) Chapter 3 – in particular 3.3 – relate to the distribution of established surplus between shareholder and policyholders. We propose to replace them with new provisions in COBS 20.2 applying to UK Solvency II firms and EEA firms where the state of the commitment is the UK) which give a similar outcome to the provisions in IPRU INS 3.3.

7.24 Part of the current rule IPRU (INS) 3.3 (1) refers to situations where the percentage of surplus allocated to policyholders is below the previous level. Changes of more than 0.5% currently need to be notified in advance to the regulator, to policyholders and the press. We propose below that this percentage is increased to 2% for prior notification, but welcome views as to what alternative boundary levels might be more appropriate.

7.25 We also propose that the requirements for advance notification to policyholders for changes of 2% or more should be in line with the requirements for changes to the PPFM principles. We further propose that smaller changes will also have to be notified but to permit this to be undertaken as soon as reasonably practical after the event.

7.26 The proposed new rules and guidance at COBS 20.2.19 AR, BR & CG also aim to achieve consistency with Solvency II concepts and terminology.

7.27 We also intend to transcribe a slightly amended version of IPRU (INS) section 3.5 which outlines requirements to avoid unfairness between separate funds where a firm operates more than one fund.

Q10: Do you agree with our proposals to amend the changes in surplus distribution notification requirements currently addressed by IPRU (INS) Chapter 3.3?

Q11: Do you agree that IPRU (INS) section 3.5 should be transcribed into COBS 20?

COBS 20.3 Principles and Practices of Financial Management (PPFM)

7.28 COBS 20.3 requires firms to establish and maintain a PPFM and prescribes the scope and content of the PPFM.

7.29 We propose that firms that wish to use support assets should adequately document the terms and conditions of their use and describe them clearly and unambiguously in their PPFM and mention them in their Customer Friendly (CF) PPFM.

Q12: Do you agree that we should amend COBS 20.3 to require Solvency II firms who wish to use support assets to document and describe them in their PPFMs?

COBS 20.4 Communications with with-profits policyholders

7.30 COBS 20.4 contains rules regarding the provision of PPFM to policyholders, on the provision and issue of a CFPPFM and on the production of an annual report to policyholders. We propose to amend COBS 20.4.4 slightly to require incoming EEA firms, where the UK is the Member State of the commitment, to provide information that is not narrower in scope or less detailed in content than the information required to be provided in the PPFM by a firm subject to the PPFM requirements. This ensures that standards for policyholders of such firms that are habitually resident in the UK at the time of sale, are broadly equivalent to those for UK firms.

COBS 20.5 Governance and responsibilities for with-profits committees

7.31 This section outlines governance requirements and responsibilities for with-profits committees to ensure with-profits policyholders are treated fairly. We propose that the existence and scope of sub-funds, and the availability and value of any support assets should be added to the list of issues that the with-profits committee or alternative governance body should consider.

Q13: Do you agree that we should amend COBS 20.4.4 and that with-profits committees should also consider the existence and scope of sub-funds and availability and value of any support assets within COBS 20.5?

GENPRU chapter 2: Capital instruments

- 7.32** GENPRU Chapter 2 currently contains provisions relating to capital instruments for firms carrying on with-profits insurance business. We propose to make new provisions in COBS 20 for Solvency II firms relating to their management of the with-profits fund that are aimed at achieving the outcome currently provided by GENPRU 2.2.271R(1) and (2) and a degree of protection not dissimilar to the current GENPRU 2.2.271R(3).
- 7.33** GENPRU 2.2.271R(1) imposes a condition on the inclusion of a capital instrument in a firm's capital resources. This condition requires that the firm's with-profits fund is managed so that discretionary benefits payments are calculated and paid disregarding payments under the instrument to the extent needed to ensure fair treatment. The proposed new COBS provision will make this a requirement on the management of the with-profits fund without making it a condition of the instrument being included as capital that qualifies as counting towards meeting the SCR.
- 7.34** GENPRU 2.2.271R(2) imposes a further condition on instruments which may count towards capital resources. It requires a firm to include in its PPFM any intention to manage the with-profits fund on the basis set out in GENPRU 2.2.271R(1). The proposed new COBS provision will require firms to include the intention to manage in this way in its PPFM without making it a condition of qualifying capital.
- 7.35** GENPRU 2.2.271R(3) imposes a condition that no amounts are payable under the instrument if the firm's assets would be insufficient to enable it to declare and pay discretionary benefits consistent with treating customers fairly. We propose to introduce new guidance in COBS 20 to the effect that firms should manage their with-profits funds so that amounts payable under instruments do not impact on a firm's ability to pay out discretionary benefits that are consistent with their treating customers fairly requirements.

Q14: Do you agree that the proposed new provisions in COBS 20 relating to GENPRU 2.2.271R(1)-(3) are appropriate?

INSPRU 1.5 Internal and contagion risk

- 7.36** INSPRU 1.5 contains a number of provisions relevant to the governance and management of with-profits business. The current description of a long-term fund, on which the definition of a with-profits fund for Solvency II firms is planned to be based, can be found at INSPRU 1.5.21R and 1.5.22R. These are followed by governance and management provisions around those rules and some additional guidance.
- 7.37** We consider that the governance and management provisions around the operation of the with-profits fund currently in INSPRU 1.5 should be made as new provisions in COBS 20.
- 7.38** These provisions are broadly:

- to have separate accounting records for with-profits business (1.5.23) and related guidance;
- restrictions on transfers out of with-profits funds (currently in 1.5.27);
- with-profits assets can only be used for with-profits business (1.5.30);
- that with-profits assets are only used to back the liabilities of with-profits business and that mortgages or charges on long-term assets are not normally permitted (1.5.31/32); and
- financial penalties that may be imposed on proprietary firms must not be paid from the with-profits fund (1.5.33).

7.39 We consider that these are necessary to protect policyholder interests as expected when they purchased their products, and the connected expectations in relation to these products (including the expectation that firms will comply with COBS 20 in the managing of assets that may have an impact on the payout to policyholders).

7.40 We propose to carry forward a requirement that firms report to us the technical provisions for each with-profits fund so that this can be related to the prior identification of the assets within the with-profits fund. The reporting will be achieved through national specific templates on which consultation will take place at a later date.

7.41 The proposed provisions in COBS 20 for Solvency II firms have been changed from current guidance in INSPRU, in part to reflect the Directive, including the following:

- the assets and liabilities of the with-profits fund will need to be separately identified and broken down by their reference to with-profits and non-profit business. This is because the non-profit business may be being used as an investment of the with-profits policyholders and so we need to be able to monitor it separately for the latter's protection;
- rather than restrict transfers of assets out of the fund (other than in connection with their with-profits business) to assets that represent an 'established surplus' (see para 2.11 above), we propose to restrict transfers of assets out of the fund to assets representing a 'with-profits fund surplus' (other than transfers of shareholder distributions);
- we will continue to require the calculations to be established for the firm by an 'actuarial investigation' (as explained in INSPRU 1.5.28); , but the firm will need to decide who prepares this investigation for them though the with-profits actuary will be required, at least, to give advice on it (see amendment to SUP 4.3.16AR);
- we have improved the wording on some of the restrictions and are also planning to clarify the existing INSPRU rules, and

- we also intend to introduce new rules regarding sub-funds to require that firms consider fairness and other relevant issues such as communications to policyholders when determining the existence and scope of a particular with-profits fund or sub-fund.

Q15: Do you agree that the governance and management provisions from INSPRU 1.5 should be converted into new rules in COBS 20 for Solvency II firms in order that policyholder interests continue to have adequate protection?

INSPRU 1.1 Assets of a value sufficient to cover technical provisions and other liabilities

7.42 INSPRU 1.1.27R requires a firm to ensure that it has sufficient assets in each with-profits fund, at all times, to cover the liabilities of that fund. INSPRU 1.1.28R provides similar requirements for realistic reporting firms. We propose a new rule in COBS 20 for Solvency II firms to require firms in managing its with-profits fund to ensure that such that assets meet liabilities within the fund.

Q16: Do you agree that we should include a new rule in COBS 20 to require Solvency II firms to manage their with-profits fund to ensure that assets meet liabilities?

Handbook glossary – definitions

7.43 We need to amend a number of definitions relating to with-profits business to ensure consistency with the Directive.

With-profits policy and insurance contract

7.44 The current definition of a with-profits policy refers to it being a class of long-term insurance business that provides for the policyholders to be eligible to participate in any part of the established surplus. Established surplus is defined in IPRU (INS) 3.3(4) and is essentially the excess of assets over liabilities as calculated under current rules. We wish to change the definition of a with-profits policy to remove reference to ‘surplus’ given its narrower scope in our rules following implementation of the Directive.

7.45 There is also a definition of a ‘with-profits insurance contract’ that is similar.¹ We propose to delete this definition and not to differentiate in future for Solvency II firms. We are also taking the opportunity to propose to clarify certain other points around the definition of a with-profit policy including:

¹ A long-term insurance contract which provides for the policyholder to be eligible to participate in any surplus arising on the whole or any part of the insurers’ long-term business.

- differentiation of with-profits contracts from unit-linked business, since the latter does not involve the exercise of discretion when determining benefits; and
- that participations expected at the outset must not be immaterial and are by way of periodic discretionary additions to benefits during the term of the policy rather than simply occurring at the point of a claim being made.

With-profits fund

- 7.46** The current definition of a with-profits fund is ‘*a long-term insurance fund (or part...) in which policyholders are eligible to participate in any established surplus*’. The concept of a long-term insurance fund does not apply in the Solvency II environment, so we must amend this definition. Also, given that the with-profits fund will in our view be treated as a ring-fenced fund, we consider that it will be important to ensure that firms take into account relevant factors that may restrict own-fund items including the way that products were represented to policyholders when determining the existence and scope of a particular with-profits fund or sub-fund.
- 7.47** As stated above, we propose to use a description of the with-profits fund based on the current description of the long-term fund in INSPRU 1.5.21 and 1.5.22R. Broadly speaking, this identifies the income and assets relating to with-profits policies (and the income and assets relating to non-profit policies in which the with-profits policies have an interest for example by way of investment) as constituting the with-profits fund.
- 7.48** There are a number of changes including those to adapt to the Directive in particular:
- there is an additional requirement in the draft definition that assets that are described in the firm’s PPFM (or in literature or other communications) as available to cover liabilities in the with-profits fund(s) form part of the with-profits fund even though they are not included in the firm’s accounting for it; and
 - we have explicitly included income and assets intended to cover liabilities in connection with non-profit business.
- 7.49** We also propose the addition of guidance to make clear that the inherited estate is included within the with-profits fund, by stating that references to premiums and other incoming funding includes items in relation to policies that have since matured or otherwise terminated. Further guidance will clarify that we do not expect non-mutual firms to hold any assets to cover subordinated debt in the with-profits fund.
- 7.50** Another change from the existing definition and provisions in INSPRU 1.5 is that firms will need to ensure that policy terms, the established practice of the firm and communications from the firm (including the PPFM) are consistent with the identity and scope of the with-profits funds and sub-funds they have in place. We propose to add to the provisions on the existence of sub-funds in our rules (currently based on the firm’s established practice and identification of assets by the firm) so that a sub-fund

can be created only if it is consistent with what all affected policyholders have been told and, in the case of conflict, if it is fair between all such policyholders. Conversely, we propose to add a provision to state that, even if a firm has not created a separate sub-fund, such a sub-fund will be deemed created if it is necessary to do so in order to treat policyholders fairly with regard to the PPFM and other policyholder communications (see proposed guidance on this point below).

- 7.51** We also propose that there should be a Handbook Transitional Provision to clarify that current with-profit funds will be ‘grandfathered’ over to be deemed to fall within the new definition. The Transitional Provision will operate so that such a transfer out before the effective date of the new rules (which would be in breach of the current rules in INSPRU 1.5 on transfers out of the fund) means that the asset is still considered a constituent of the with-profits fund. If a firm has transferred assets out of the fund in breach and then also transferred the assets out of the firm, the transitional provision will not be available until the firm has restored assets of equal value and quality into the fund. However, even if a firm is able to rely on this transitional provision, it will still need to ensure it has its split of funds or sub-funds appropriately constituted. A firm will therefore still need to consider whether it is appropriate to create new sub-funds or merge existing sub-funds based on the requirements in the new rules. It is proposed that the transitional provision will last for one year.

With-profits assets

- 7.52** The definition of with-profits assets is currently ‘assets that match liabilities in respect of *with-profits insurance business* or represent a *with-profits surplus*’.
- 7.53** The definition of with-profits surplus, though italicised, is not a defined term. It is proposed that reference to it is deleted and updated for Solvency II firms to adapt to the Directive. The definition for out of scope Solvency II firms will be amended to achieve consistency. We also propose to change the definition to reflect the changes to the definition of the with-profits fund, which requires certain assets to be treated as included.

Inherited estate

- 7.54** The inherited estate is currently defined as ‘an amount representing the fair market value of the *with-profits assets* less the *realistic value of liabilities* of a with-profits fund’. This is the surplus in the with-profits fund – including the working capital required for the capital requirements of current business and also for the requirements of reasonable levels of future new business.
- 7.55** For out of scope Solvency II firms we intend to clarify that, for a firm that is not a realistic reporter, it is the regulatory value of liabilities that is relevant. We also propose that for Solvency II firms we replace references to realistic values of liabilities with the corresponding references to technical provisions and other liabilities calculated in accordance with new SOLPRU provisions.

Miscellaneous issues

With-profits funds are ring-fenced funds

- 7.56 We propose to give guidance in COBS that, in our view, with-profits funds and sub-funds should be treated as separate ring-fenced funds for the purpose of the Directive.

Rules to collect data on assets and technical provisions for each individual with-profits fund

- 7.57 We will need to have a rule in the Handbook to specify the reporting to us of each item above those included in the standard templates, in order to comply with Articles 35 and 254 (2) of the Directive on the collection of National Specificities. The purpose of this proposed rule is to enable us to identify separately all the assets of each with-profits fund to ensure that we can appropriately relate them to the technical provisions in each fund. Equally, we propose to require firms to report the technical provisions for each with-profits fund in the firm separately to allow us to monitor and supervise the rules proposed previously in this chapter.
- 7.58 The consultation on the detailed form of the National Specific Templates data collection requirements will take place in a later consultation.

Q17: Do you agree with our proposals to amend definitions, as above, and to introduce a transitional provision (para 7.51)?

Amendment of existing transitional provision

- 7.59 The current COBS 20 rules include a Transitional Provision COBS TP2.9. This permits firms with (sub-) funds that had been transferred to them under Court Schemes (e.g. Part VII/FSMA transfers, schemes of arrangement or demutualisations), or transfers approved by the FSA or previous regulators, on or before 20 January 2005 to not have to comply with the rules after they were introduced on 1 November 2007 where there was a conflict with COBS 20.
- 7.60 This means that the protection given to those consumers is potentially less than for other consumers to which the rules apply. This refers to all of COBS 20 except the rules dealing with reattributions. We note, however, that TP2.9 mentions that a firm should be mindful that, even if some or all of these rules are disapplied, the firm is still subject to the rules in the rest of the Handbook, including Principle 6.
- 7.61 Although there are a significant number of funds affected by TP2.9, we wish to ensure that consumers invested in those funds will in future enjoy similar rights to other with-profits policyholders.

- 7.62** In particular we would like to make sure that if any schemes are brought back to court by firms for whatever reason, that such firms request that the court reviews the continuing appropriateness of their reliance on the transitional provision with the FSA and, if appropriate, request that the court agrees that the scheme should become fully compliant with the current rules.
- 7.63** In view of the significance of this transitional provision to policyholder protection, we propose to implement this change from 31 March 2013 ahead of Solvency II implementation.

Q18: Do you agree that firms should be required to ask the court to review the appropriateness of their continued reliance on the transitional provision with the FSA when bringing a scheme back to court?

Surplus funds (Article 91 of the Directive)

- 7.64** In CP11/22 we introduced the concept and a proposed definition of *approved surplus funds* but made it clear that we were still considering the extent to which surplus funds should be recognised in our Handbook rules. We are now proposing the introduction of rules within SOLPRU that will allow approved surplus funds to be excluded from technical provisions and will specify the basis of determining which amounts have been made available for distribution to policyholders, to be taken into account when calculating technical provisions, and which amounts have not and therefore constitute approved surplus funds. These rules will constitute the relevant national law for the purposes of Article 91 of the Directive.
- 7.65** Our rules on surplus funds are confined to with-profits business. The definition of ‘approved surplus funds’ has been amended to incorporate references to the proposed rules and to remove the requirement for a waiver.
- 7.66** Our proposed rules will require the calculation of the value of the asset share for with-profits policies and additions to or deductions from this value to take account of the costs of guarantees and options, smoothing and certain other items that will affect future policy benefit payments. An alternative calculation methodology will apply where asset share is not appropriate. These calculations will draw on the concepts currently reflected in INSPRU 1.3.118 et seq. and will support the determination of approved surplus funds.
- 7.67** However, in addition to being derived as described above, approved surplus funds will also need to satisfy SOLPRU 3.3.2R regarding the criteria for classification as Tier 1 own funds. And despite their classification status, approved surplus funds may be subject to restrictions and ring-fencing adjustments because of their existence in a with-profits fund and the requirements in COBS on the fair treatment of policyholders. We propose to introduce guidance clarifying the interplay of these requirements.

Q19: Do you agree with the proposed rules which specify the determination of assets shares, or equivalent calculations, in order to calculate approved surplus funds?

Q20: Do you agree with our revised definition of approved surplus funds and the proposed guidance on classification?

Cost benefit analysis

7.68 Most proposed changes outlined in this chapter are intended to make consequential and largely technical changes to the current rules so that they are consistent with Solvency II and not to make material changes to our requirements.

7.69 The baseline for the cost benefit analysis is our current rules and guidance on the operation of with-profits insurance policies. These include (COBS) 20 With-profits, and some rules on the governance of with-profits business that are currently in IPRU (INS), GENPRU and INSPRU.

Application of COBS 20 (COBS 20.1.1-5)

7.70 As the rules are largely unchanged, there will be no significant cost and benefit implications.

Introduction to Treating with-profits policyholders fairly (COBS 20.2.1-2)

7.71 As the rules are unchanged, there will be no cost and benefit implications.

Amounts payable under with-profits policies (COBS 20.2.3-16)

7.72 As the changes are limited to glossary definitions and cross-references to new corresponding provisions in SOLPRU, the underlying requirements are unchanged, and we expect there will be no incremental costs and benefits.

Conditions relevant to distributions (COBS 20.2.16B-20)

7.73 The proposed guidance (COBS 20.2.16B), and the proposed amendments to rules (COBS 20.2.17 and 2.18), aim to address the valuation of future reversionary annual bonuses for conventional with-profits business to calculate the balance of the distribution between policyholders and others in the Solvency II regime. As the guidance and the proposed amendments aim to maintain the current requirements on conditions relevant to distributions, we expect there will be minimal incremental costs and benefits.

Requirements relating to distribution of an excess surplus (COBS 20.2.21-22)

- 7.74 As the proposed amendments are designed to achieve the same outcome as current requirements, we expect there will be minimal incremental costs and benefits.

Charges to a with-profit fund (COBS 20.2.23-27)

- 7.75 As the proposed introduction of a provision (COBS 20.2.26A) for Solvency II firms replaces the current rule INSPRU 1.5.33R, the provision COB 20.2.26A should have the same effect as the current rule INSPRU 1.5.33R, we expect there will be no incremental costs and benefits.

New business (COBS 20.2.28-31)

- 7.76 As the rules are unchanged, there will be no cost and benefit implications.

Connected persons (COBS 20.2.32)

- 7.77 We propose to disapply this rule for Solvency II firms as granting a loan using assets in the with-profits fund is likely to be regarded as an investment of those assets and therefore covered by the Prudent Person Principle. It is expected that the proposed new guidance, and the implementation of the Prudent Person Principle, should have the similar effect of the current rule for loans made to connected persons using assets in the with-profits fund. Therefore we expect there will be minimal incremental costs and benefits.

Contingent loans and other support (COBS 20.2.33-34)

- 7.78 The proposed new rule (COBS 20.2.34A) on support assets will lead to some additional costs for firms because of having to adequately record and explain to policyholders, including in their PPFM, the terms and conditions, including the circumstances in which repayment will be required. However, we do not expect the costs to be significant. We estimate that for each firm, that does not already disclose, it could take several working days to draft and review PPFM and CFPPFM. We further estimate that this will involve 10 to 20 firms. This improved disclosure could help ensure the fair treatment of policyholders. Overall, we do not expect this would lead to significant incremental costs and benefits.

Other rules and guidance on the conduct of with-profits business (COBS 20.2.35-38)

- 7.79 The proposal to dis-apply current rules and guidance about investment strategy and strategic investments will have minimal cost and benefit implications as this issue will be covered by the Prudent Person Principle.

- 7.80 The proposal that the provisions implementing the Prudent Person Principle should be applied at with-profits fund level aims to maintain the status quo where the COB rules are applied at with-profit fund level.
- 7.81 Therefore we expect there will be minimal cost and benefit implications.

Major changes in with-profits funds including the process for reattribution (COBS 20.2.39-20.2.52)

- 7.82 As the rules are unchanged, there will be no cost and benefit implications.

Ceasing to effect new contracts of insurance and run off plans (COBS 20.2.53 – 20.2.60 and SUP Appendix 2.15)

- 7.83 The proposed amendments (e.g. terminology changes for the balance sheet) do not change the underlying regulatory requirements in this area. Therefore we expect there will be minimal cost and benefit implications.

Principles and Practices of Financial Management (PPFM) (COBS 20.3)

- 7.84 Firms that wish to use support assets should adequately document the terms and conditions of their use and describe them clearly and unambiguously in their PPFM and mention them in their Customer Friendly (CF) PPFM. The cost and benefit implications have been discussed under ‘Contingent loans and other support’ (COBS 20.2.33-34) in paragraph 7.78.

Disclosure of change in distribution IPRU (INS) 3.3

- 7.85 Currently, when the percentage of surplus allocated to policyholders is to be 0.5% below the previous level, the insurers are required to give the FSA written notice and publish a statement in the *London, Edinburgh and Belfast Gazettes* and in two national newspapers explaining the allocation proposed to policyholders and the reasons for it.
- 7.86 The proposed amendments (COBS 20.2.19) require advanced notification to policyholders for changes of 2% or more, and are in line with the requirements for changes to the PPFM principles, while permitting smaller changes to be notified as soon as reasonably practical after the event.
- 7.87 We do not expect this will lead to significant costs and benefits. This is because (1) firms are still required to give prior notification to the FSA of any reduction in the percentage of surplus allocated to policyholders even when the change is smaller than 2%; (2) nearly all funds are at 90/10 limit already and are therefore unlikely to change; and, (3) the current disclosures entail publishing a statement in the *London, Edinburgh and Belfast Gazettes* and in two national newspapers, which we do not consider as effective in communicating with policyholders.

Communications with with-profits policyholders (COBS 20.4)

- 7.88** The proposal to require incoming EEA firms to provide ‘information equivalent to that which is in the PPFM’ will incur some costs for incoming EEA firms that are not already providing PPFM equivalent information. However, to the extent that PPFM has been useful in providing the necessary information to financial advisers (and CFPPFM has been useful in providing the necessary information to policyholders) and for the FSA to assess and evaluate, there are benefits for UK policyholders of incoming EEA firms. We note that there are few such cases.

Governance and responsibilities for with-profits committees (COBS 20.5)

- 7.89** The proposal that with-profits committees should also consider the existence and scope of sub-funds and the use of support assets will lead to some additional costs for the running of with-profits committees. However, we do not think the additional costs will be significant.

Capital instruments GENPRU Chapter 2

- 7.90** The proposed COBS 20.1A.13R-14G provisions aim to maintain the existing requirements set out currently in GENPRU 2.2.271 without overlapping with Solvency II, so we expect there will be minimal incremental costs and benefits.

Internal and contagion risk INSPRU 1.5

- 7.91** Some proposed provisions in COBS 20.1A aim to import the current governance and management provisions from INSPRU 1.5, and therefore we expect there will be minimal cost and benefit implications.
- 7.92** The proposed rule requires firms to calculate the technical provisions for each with-profits fund separately. This is a current requirement in INSPRU 1.5, and therefore has no cost and benefit implications.

Assets of a value sufficient to cover technical provisions and other liabilities INSPRU 1.1

- 7.93** This proposed new rule COBS 20.1A.5R, requiring firms to manage their with-profits fund such that assets meet liabilities within the fund, aims to import the requirement currently in INSPRU 1.1.27-28, and therefore has no cost and benefit implications.

Handbook glossary – definitions

- 7.94** The proposed amendments, in the main, aim to ensure consistency with Solvency II, and not to make any significant changes in regulatory requirements. Therefore we do not expect there will be significant cost and benefit implications.

With-profits fund – transitional provision

- 7.95** The proposed transitional provision is to ensure that current with-profits funds will be grandfathered over to be deemed to fall within the new definition. This means that assets transferred out in breach of the rules in INSPRU 1.5 will still be considered a constituent of the with-profits fund. This has no significant cost and benefit implications.

Rules on approved surplus funds

- 7.96** The use of the surplus funds concept in the way described ensures that own funds consisting of assets that have not (yet) been made available for distribution are not absorbed by the technical provisions, and are therefore available to cover the SCR and demonstrate solvency. The non-inclusion of such assets is appropriate given that they would be available to cover the contingencies underlying the SCR.
- 7.97** The use of the concept of surplus funds should not lead to additional compliance cost for firms. We also do not expect that the use of the concept of surplus funds would of itself lead to a change in the capital requirements of undertakings.
- 7.98** In addition, we do not expect this to make any significant difference to the payouts that with-profit policyholders will receive as distributions to policyholders will be supervised in accordance with the new COBS 20 conduct rules.

8

Linked long term insurance business – derivatives, stock lending and governance

Introduction

- 8.1 In CP 11/23 *Solvency II and linked long-term insurance business*, we consulted on most of the changes deemed necessary for the rules relating to such business, primarily in COBS 21 *Permitted Links*. In doing this our intention was to implement the Directive's new requirements while maintaining an appropriate level of consumer protection. We were unable to cover in that CP how we proposed to deal with issues related to derivatives, stock lending, and governance because of continuing uncertainty on the likely outcome of work on these areas at an EU level.
- 8.2 In this chapter we set out our proposals to amend COBS 21 where derivatives are used for purposes other than efficient portfolio management and the reduction of risks. That is, where policy benefits are linked to the performance of derivatives. We will do this for policies taken out by policyholders and on behalf of beneficiaries who are natural persons and bear the direct investment risk of the assets. We propose to introduce guidance that sets out our view that good practice will involve firms following the requirements for the use of derivatives set out in COLL 5.3.
- 8.3 We also propose to retain a modified form of the rule, currently in INSPRU 3.2.36AR, relating to stock-lending assets backing unit-linked policy benefits.
- 8.4 The outstanding process for the adoption of Solvency II's Level 2 regulations are set out in chapter 2. We think there is now sufficient clarity and stability at EU level on the specific issues covered in this chapter to be able to consult on this material. In doing so we are mindful of the need to give firms as much certainty as we can on the eventual

contents of the Handbook, although we also note the risk of amendments to the texts we are relying on.

- 8.5 We do not propose to bring in any further requirements on systems of governance at this time.

Derivatives

- 8.6 The use of derivatives in unit-linked funds is currently subject to INSPRU 3.2, *Derivatives in insurance*, which sets out detailed requirements and puts in place cover requirements. INSPRU is being replaced by SOLPRU, for Solvency II firms, which does not contain rules of equivalent detail.
- 8.7 Currently, derivatives and quasi-derivatives can only be used for the purposes of efficient portfolio management (EPM) or to facilitate reduction of investment risk (RoIR).² The Directive removes this restriction on the uses of derivatives for unit-linked funds that do not contain any guarantees. The RoIR restriction will be altered to become Reduction of Risks (RoR).
- 8.8 In addition to the limited changes described above, there is also a widening of the range of assets firms can use to back linked business. In particular, where policyholders are not natural persons (in practice trustees of defined benefit (DB) occupational pension schemes), there will be no restricted list of assets so there will be a far greater range of assets available to be used. SOLPRU 7 (the Prudent Person Principle) and the revised COBS 21.2 apply to all of the assets and derivatives being used.
- 8.9 The removal of the restrictions on the use of these financial instruments will allow firms to link policy benefits to investment strategies that use derivatives rather than using them for EPM or RoR. This change is set out in SOLPRU 7.2.10R. We also remove the requirement for all other business to keep assets not admitted to trading on regular markets at prudent levels, as well as the requirement to properly diversify assets. All of the other requirements of the Prudent Person Principle will apply.
- 8.10 The removal of the need to keep assets not admitted to trading on regular markets at prudent levels also has consequences for the assets firms may use, for example, over-the-counter (OTC) derivatives can be used.
- 8.11 The need for assets to be secure, as required by Article 132 (2) leads us to believe that firms must continue to have cover in place for all derivative use. We do not think the relaxation of the restrictions on the use of derivatives should allow firms to link policy benefits to derivatives, without some controls, where the policyholder or beneficiary is a natural person who bears the direct investment risk. We propose to amend the definition

² Directive 2002/83/EC Article 23 (3) (iv)

of a ‘permitted derivative’ in COBS 21.3 to refer to the restrictions on derivative use set out in the COLL rules.

- 8.12** For business where the ultimate beneficiary does not bear the direct investment risk, the restriction on the assets to which benefits may be linked does not apply. Instead any financial or other asset, for example, commodities, that can pass the tests imposed by SOLPRU 7 and the revised high level rules in COBS 21.2 can be used. So derivatives based on these assets will also be permitted. This relates primarily to policies effected by trustees of defined benefit occupational pension schemes. Where the policyholders or beneficiaries are natural persons who bear the direct investment risk, then Article 133(3) allows us to restrict the type of assets to which policy benefits can be linked.
- 8.13** We propose to take an approach that recognises the different uses of derivatives as well as whether the policyholders and beneficiaries bear the direct investment risk. It should be noted that, while Article 132(4) allows the wider use of derivatives in unit-linked funds it does not remove any of the other requirements relating to the way in which firms are required to identify, measure, monitor, manage, control and report on them. Firms holding derivatives for any purpose must comply with these requirements and those set out in Article 44(2)(c) on risk management in relation to derivatives and similar commitments.
- 8.14** One of the duties of the governance function will be to report on how this is done under Article 35, which relates to the provision of information to supervisors. Firms will have to demonstrate how any derivatives they hold conform to all the relevant requirements of Article 132, for example, only investing in instruments they can properly identify, measure and monitor so as not to compromise their ability to meet their obligations to, or conflict with the interests of, policyholders and beneficiaries.
- 8.15** We take the view that where firms continue to use derivatives on the current basis and maintain their current systems and controls then they are likely to be meeting the new requirements and we do not propose to put any new rules into the Handbook.
- 8.16** Article 75 of Solvency II also puts requirements on firms in relation to valuing their assets and liabilities, which apply equally to derivatives.
- 8.17** These requirements are in addition to those described above for firms using derivatives for more limited purposes, as well as the rules in SOLPRU 7, COBS 21 and SOLPRU 9 transposing the governance requirements. As a result we do not propose to put any new rules in the Handbook.
- 8.18** The changes under the Directive allow the creation of unit-linked funds that operate in a very similar way to the UCITS Directive. This already permits funds offered to retail investors to use derivatives for wider investment purposes.

- 8.19** The relevant requirements in the UCITS Directive³, transposed into COLL 5.3, *Derivative exposure*, represent, we believe, good practice and ought to be applied where derivatives are used in the way described above in unit-linked funds. We propose to modify the definition of permitted derivatives in the Handbook and introduce guidance into COBS 21.3 that refers to the COLL guidance. In particular we propose to refer to the rules, amended as appropriate, in:
- COLL 5.3.3A on cover for investment in derivatives and forward transactions;
 - COLL 5.3.3B and C on daily calculation of global exposure;
 - COLL 5.3.5R on borrowing amended as appropriate; and
 - COLL 5.3.7R and 5.3.8R on calculation of global exposure.
- 8.20** We note that firms will also have to comply with the requirements of what was previously referred to as EMIR, the European Market Infrastructure Regulation, where relevant and to note the joint discussion paper from EIOPA, ESMA and EBA in relation to risk mitigation techniques and OTC derivatives.⁴

Cost benefit analysis

- 8.21** Where institutional policyholders are concerned, there could be benefit from the removal of restrictions on how derivatives are used in unit-linked policies. There may, however, be some compliance costs associated with using derivatives in unit-linked funds but firms would only incur these costs if they decided to offer them. We do not anticipate that the greater freedom in the use of derivatives will lead to material detriment to members of defined benefit schemes. As our earlier analysis of market failures⁵ showed that these consumers are at lower risk of detriment than retail consumers. This is because the overall financial position of institutional-linked policyholders does not necessarily have a direct impact on the benefits of its individual members.⁶
- 8.22** Where retail policyholders are concerned, again, there could be benefits from the removal of restrictions on how derivatives are used in unit-linked funds, and firms would only incur related compliance costs if they decide to offer them. We are mitigating the potential costs of detriment to retail policyholders by introducing guidance into COBS 21.3 that refers to the COLL guidance on derivative usage. In addition, the risk of retail policyholders being exposed to excessive risk is further mitigated by the requirements of

³ Including the European Securities and Markets Authority's guidelines: Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS.

⁴ Joint Discussion Paper on Draft Regulatory Standards on risk mitigation techniques for OTC derivatives not cleared by a Central Counter Party under the Regulation on OTC derivatives, CCPs and Trade Repositories (JC/DP/2012/1) 6 March 2012.

⁵ Annex 3, CP 11/23: www.fsa.gov.uk/static/pubs/cp/cp11_23.pdf

⁶ The reason for this is individual members receive guaranteed benefits for which the sponsoring employer is responsible for remedying any funding shortfalls. In theory, there could be a risk to DB pension members and Pension Protection Fund should institutional policyholders not meet obligations as a result of misguided use of derivatives. However, we do not think this risk is significant as there will be implications for creditworthiness for the DB pension sponsors if/when they default on their pension liabilities.

the Prudent Person Principle. For example, firms will have to demonstrate how any derivatives they hold conform to all the relevant requirements of Article 132.

Q21: Do you agree with our proposals for the use of derivatives?

Q22: Do you agree with our proposal to amend COBS 21 to refer to the requirements of COLL 5.3 where funds using wider investment powers are offered to policyholders and beneficiaries who are natural persons and bear the direct investment risk?

Stock lending

- 8.23** Stock lending is a permitted activity in COBS 21 and will continue to be so when the Directive takes effect. In common with derivative use, it is subject to detailed rules in INSPRU 3.2.36R relating to, for example, approved counter-parties and collateral, which will be discontinued and replaced with the higher level requirements in the Directive.
- 8.24** The Directive texts do not contain any specific reference to this activity but, in common with all other linked assets, their uses are subject to all of the requirements of SOLPRU 7, SOLPRU 9 and COBS 21.2. While the detailed rules referred to above are not carried over, we would question how firms not ensuring the fitness of their counter-parties and not putting in place collateral as they do now could be assessed as meeting the requirements of the Prudent Person Principle.
- 8.25** These requirements lead us to take the view that the application of the Prudent Person Principle under the Directive amounts to at least an equivalent requirement to the current rules in INSPRU.
- 8.26** Where the assets lent are permitted links, they are also subject to INSPRU 3.2.36AR(d), which says that where the assets being lent are permitted links then policyholders and beneficiaries must receive all of the recompense, less fees and expenses, and any risk associated with the transaction must be clearly disclosed to them. This rule was put in place in 2007 to ensure the fair treatment of policyholders and we propose to copy this rule into COBS 21 in order to ensure this important protection continues.
- 8.27** We propose to rely on the requirements described above in relation to stock lending and would consider the maintenance of current practice, as amended, to meet any extra requirements firms have identified to comply with the Directive, as likely to demonstrate compliance. However, where the policyholders and beneficiaries are natural persons and bear the direct investment risk, we also propose to adopt some of the rules in COLL 5.4 on stock lending, amended as appropriate. In particular we propose to use COLL 5.4.4R

on stock lending requirements and COLL 5.4.6R on the treatment of collateral. We note that in most respects the requirements in COLL 5.4 are very similar to the current INSPRU requirements. We also propose to put the current INSPRU 3.2.36AR into COBS 21, again, to ensure this important protection continues.

Cost benefit analysis

8.28 As we are proposing to maintain the effect of the current requirements in relation to stock lending, we do not expect there will be significant cost benefit implications.

Q23: Do you agree with our proposals on stock lending?

Q24: Do you agree that our proposals maintain the effect of the current level of protection in place in relation to stock lending for policyholders and beneficiaries?

Governance

8.29 The Directive contains extensive requirements on the systems of governance firms must have in place that all Solvency II firms must comply with. These are contained in Articles 41 to 50 of the Directive. Article 41 requires firms to have effective, clearly defined and transparent governance arrangements that are reviewed regularly to provide for the sound and prudent management of their business and are proportionate to the nature, scale and complexity of that business. These are set out in the proposed text of SOLPRU 9.2.3R to 9.2.9R as consulted on in CP11/22.

8.30 It follows that firms must put in place systems of governance that are appropriate for the particular types of business they write in order to be able to take account of the particular risks that they carry. All of the material risks identified by the firm will then have to be addressed within the ORSA.

8.31 As a result, at this stage we do not propose to introduce any further rules on governance but will review this as necessary.

8.32 Further, the Directive is explicit that firms set up their systems of governance in such a way that they are available for supervisory scrutiny.

8.33 Bearing in mind the results of the survey discussed below, we do not believe it is necessary to bring forward any proposals for guidance for firms in this area.

Cost benefit analysis

8.34 We have carried out research on firms' current system of governance in place for linked business and how well the current system will comply with the requirements of Solvency II. The research surveyed 18 firms of all sizes, both proprietarily and mutually owned, some writing new unit-linked as well as other business and some running closed funds only. We thank the Association of Financial Mutuals for their help in this work.

8.35 All respondents said that they have assessed their current governance arrangements in light of the Directive and concluded that their arrangements were either appropriate already or require only some small adjustments⁷. Therefore we do not expect there will be significant cost or benefit implications.

Q25: Do you agree with our view that the Directive provides appropriate protection for unit-linked policyholders and beneficiaries?

Q26: Do you agree with the assessment of the appropriateness of the systems firms currently have in place? Do you agree that no further guidance is required?

⁷ One feature of all of the responses is that the work on unit-linked business is just one part of the system of governance that needs to be in place. As a consequence no firms were able to identify the exact cost relating to the unit-linked work in isolation. Some said continuing uncertainty in relation to Levels 2 and 3 prevented an overall cost assessment while others said the cost would not be material.

9

Consequential amendments to Handbook

Introduction

- 9.1** This chapter seeks views on a proposed series of technical changes and refinements to ensure the introduction of rules for Solvency II results in a coherent and consistent Handbook. These cover:
- i) the application statement which sets out the scope of application, including the relevant exemptions, in respect of the Solvency II sourcebook, SOLPRU;
 - ii) consequential amendments for Solvency II firms to SOLPRU and other sourcebooks of the Handbook;
 - iii) consequential amendments for incoming EEA firms; and
 - iv) consequential amendments for out of scope Solvency II firms.
- 9.2** We also propose some new draft consequential rules in SOLPRU in transposing the Directive. At the end of the chapter, a table summarises the impact of the proposed sourcebook changes on different categories of insurance firm, the full list of draft rules and guidance being set out in Appendix 6.

Application statement

- 9.3** The proposed text for SOLPRU 1.1 defines the general scope of application for SOLPRU, namely all insurers with a head office in the UK, but with the exception of firms that come within some defined exclusions under the Solvency II Directive.

- 9.4 These exclusions relate primarily to certain small firms that meet the size and other criteria set out in Article 4 of the Directive. The proposed text sets out one method, by a combination of rules and seeking waivers to those rules, by which we could implement Article 4 of the Directive and the various ways in which a firm can fall in to or out of the scope of Solvency II.
- 9.5 There are also some possible exclusions set out in Articles 5 to 11 of the Directive for firms with a limited range of operations. These are largely recast from previous insurance directives with certain modifications. Some of these exclusions are either not relevant to UK firms or are already implemented by the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001. Where we are required to implement an exclusion, we are considering the appropriate tool to recognise such firms as being excluded from the scope of SOLPRU. This may be through either (1) a restriction or limitation on its permissions, or (2) a waiver or modification to the rules. We shall also consider further any possible grandfathering arrangements in advance of the implementation of Solvency II and finalise this in further consultation.
- 9.6 We shall also consider further whether we should have some type of ongoing notification or confirmation regime for out of scope firms that have previously come within the size thresholds set out in Article 4 of the Directive, or have otherwise been deemed to be excluded from the scope of Solvency II, in order to be able to determine whether they should remain outside the scope of SOLPRU.
- 9.7 Firms that are excluded from the scope of SOLPRU will instead come within the scope of existing Handbook rules, including IPRU (FSOC) in the case of friendly societies, and INSPRU, IPRU(INS) and GENPRU in the case of other firms.

Consequential amendments for Solvency II firms

SOLPRU

- Solvency II firms are proposed to be excluded from the scope of Handbook requirements that concern matters covered by the Directive, as transposed into SOLPRU (see, for example, amendments to GENPRU, SYSC, INSPRU, IPRU(FSOC), IPRU(INS) and SUP);
- Appropriate cross-references to SOLPRU are added where relevant in other sections of the Handbook;
- Relevant rules are proposed to be added to SOLPRU for the pre-issuance notification to us of capital instruments as described below:

High level standards

- Consequential amendments to the application of GENPRU 3 are proposed for financial conglomerates which will apply in relation to Solvency II firms; the amendments proposed to the cross-sector rules have the effect of (i) excluding (re) insurers which are not Solvency II firms from the scope of conglomerate regulation and (ii) applying SOLPRU 11 rather than INSPRU 6 in calculating capital adequacy requirements for insurance-led conglomerates. Further changes to GENPRU 3 to adapt it to the Solvency II regime will be developed in conjunction with proposals to transpose Directive 2011/89/EU on amendments to the financial conglomerates directive (FICOD 2), which is due for transposition from 10 June 2013;
- Changes are proposed to align the application of SYSC 12 for Solvency II firms with their position under the Directive, namely that those provisions of SYSC that implement the Financial Conglomerates Directive (FICOD) still apply, but other provisions do not;
- Amendments are proposed to reflect the removal of Lloyd's from GENPRU and INSPRU, including changes to IPRU(INS). In general terms consequential amendments for Solvency II firms also apply with respect to the Society and, where relevant, managing agents also;

Prudential Standards

- Provisions relating to premiums for new business (replicated from INSPRU 1.1.41) and restricting the business of insurers and reinsurers (replicated from INSPRU 1.5.13-13B) have been added to SOLPRU as they have been recast into Solvency II;
- Community co-insurance provisions have been moved from INSPRU to SOLPRU as they are only relevant to Solvency II firms;

Regulatory Processes

- A requirement is proposed within SUP 4 for a Solvency II firm to appoint an external actuary if the firm does not have the internal capability to provide the actuarial function in accordance with SOLPRU 9.6.1;
- Retention is proposed with suitable consequential amendments to the wording of the rules and guidance in SUP App 2.8 to 2.10 and 2.12 to 2.15, relating to the provision to the FSA of a scheme of operations when a firm is seeking a variation of its permissions, or goes into run-off, or if there is a change in shareholder control, but it is proposed to disapply SUP App 2.4 to 2.7 and 2.11 for UK Solvency II firms; and
- A further consultation will consider the application of the reporting requirements that are currently set out in SUP 15 and 16 for solo firms, groups and conglomerates.

Consequential amendments for incoming EEA firms

High level standards

- Changes are proposed to the application of the Handbook to incoming firms, where necessary to reflect Directive requirements (see, for example, changes to SYSC and FIT); and

Regulatory Processes

- New references to the Directive are inserted, as required (see, for example, changes to SUP chapters on passporting).

Consequential amendments for out of scope firms

- Some Handbook provisions applying to out of scope Solvency II firms are proposed to be amended, including the removal of groups and conglomerates requirements and various provisions pursuant to this (see, for example, changes to GENPRU, INSPRU, IPRU(INS), SYSC 12), and the changes described below in relation to equalisation provisions and in relation to the currency denomination of amounts currently expressed in euros.
- Amendment of the Glossary definitions is proposed in relation to friendly societies such that these will be either Solvency II firms (and subject to SOLPRU) or out of scope Solvency II firms (and subject to IPRU(FSOC)). Previously directive friendly societies were subject to GENPRU/INSPRU and IPRU(INS), as well as to parts of IPRU(FSOC); and
- References to existing insurance directives (repealed by Solvency II) are updated or removed.

Cost benefit analysis

- 9.8 In the main, these proposed changes are of a minor or technical nature in either switching off or recasting provisions to distinguish between Solvency II and other insurers. The costs and benefits of firms' compliance with SOLPRU rules were analysed in CP11/22.
- 9.9 Where we are removing SUP, IPRU(INS), IPRU(FSOC), INSPRU, GENPRU, FIT and SYSC rules that overlap with Solvency II requirements we expect standards of policyholder protection to be at least maintained because of the effect of the package of rules the Solvency II Directive is introducing. Firms will, however, benefit from having only a single set of requirements to fulfil. In other cases where we are recasting or

maintaining existing rules or exchanging Solvency I references for Solvency II references in those parts of the Handbook listed above we expect no material incremental costs and benefits to arise.

- 9.10** To the extent that application of Solvency II by the Home State to firms that operate in the UK differs from our current standards in FIT and SYSC there could be costs and benefits, but we do not expect them to be significant.
- 9.11** For firms out of scope of Solvency II, but within Solvency I, our existing rules apply, with the exception of those which currently fall within the Insurance Groups Directive and the Financial Conglomerates Directive, and those described further below. Our data on the population of out of scope firms that apply these (group) requirements currently show that costs and benefits from the changes will not be material.

Capital instruments: pre-issuance notification

- 9.12** In CP 11/1 we consulted on a requirement that, from 1 February 2012, all firms that calculate their regulatory capital under the General Prudential sourcebook (GENPRU), including all insurers (other than certain friendly societies and certain non-UK firms), must notify the FSA before issuing any capital instrument that they wish to include as regulatory capital, either at solo or group level. The final rule was made in the Capital Instruments (Notification) Instrument 2011, which was published in Handbook Notice 114.
- 9.13** At solo level, pre-issuance notification will in most cases be required one month before the intended date of issue. However, for certain capital instruments (such as ordinary shares and new tranches of capital instruments issued under pre-notified debt programmes), notice must be given at any time up to, but not later than, the issue date.
- 9.14** We now intend to replicate the relevant GENPRU provisions as follows to apply to Solvency II insurers:
- GENPRU 2.2.61 A R to 2.2.61 H G (and consequential changes in Schedule 2) replicated in SOLPRU 3.3 (Classification and eligibility of own funds), and
 - INSPRU 6.1.43 A R to 6.1.43 F R (and consequential changes in Schedule 2) replicated in SOLPRU 11.3 (Group solvency: general provisions).
- 9.15** In so doing, we propose to amend the rule to the extent that notification should include confirmation from ‘the governing body’ rather than ‘senior management’ (the former being a more precise and identifiable definition of where responsibility lies, encompassing senior management, as per our glossary guide). The amended rule will also require that the instrument complies with the eligibility requirements for the intended tier of capital as originally signposted in CP11/1.

Cost benefit analysis

- 9.16 As we are retaining the substance of the existing rules we consulted on and published in Handbook Notice 114 there will be no incremental costs or benefits. To summarise the CBA published in the Notice, we did not expect material incremental costs since many firms already discuss planned capital issuances with the FSA and those who did not were expected to be able to notify us of plans early in the instrument development process. The requirement ensures that the FSA can discuss potential issuances with firms and address matters of concern, as well as enabling us to monitor changes to the quality of capital and minimise the potential for inappropriate terms to become entrenched.

Special provisions for out of scope firms

- 9.17 Our general approach to consequential changes is to retain, as far as possible, any provision that is or could be applicable to out of scope firms or NDFs.
- 9.18 Despite this general presumption, some consequential changes are required to many sections of the Handbook (in particular in GENPRU and INSPRU). This is because the rules and guidance often refer to, or are built on, the current Solvency I requirements. As these requirements will fall away, amendments are required to ensure those provisions retained in the Handbook make sense. Similarly, some application and substantive rules are premised on existing exclusions from the Solvency I regime. As the Solvency II exclusions in Articles 4 to 12 do not precisely match those existing exclusions, amendments will be required to ensure there are no unintended consequences for the prudential requirements of existing firms in the alignment of those exclusions.
- 9.19 From a prudential perspective, it is important to ensure that existing firms that fall out of scope of Solvency II on implementation still hold adequate capital to cover the risks associated with meeting claims on their insurance business, taking account of these risks in a suitably proportionate manner. The treatment of any newly authorised firms that will be out of scope of the Directive when they are authorised will be dealt with at a later stage.
- 9.20 Consistent with this approach, we propose the following rule amendments:

INSPRU 1.4 – Equalisation provisions

- 9.21 INSPRU 1.4 sets out the rules and guidance for UK general insurance (GI) firms⁸ to calculate and maintain equalisation provisions, in respect of specified classes of business, including in particular credit insurance business for which there was a directive requirement under Solvency I.⁹ Solvency II firms will not be required or expected to hold equalisation provisions and they will, instead, be subject to new capital requirements for

⁸ Other than non-Directive friendly societies.

⁹ These equalisation provisions are calculated on a formulaic basis by reference to historical firm specific data, rather than through a forward looking assessment of the underlying risks.

the purposes of capital adequacy and risk management. These requirements are designed to ensure a forward looking assessment of risk, and contrast with the current rules for equalisation provisions which are more mechanistic.

- 9.22** In light of this, we propose removing all the rules in INSPRU 1.4, so that no firm (including Lloyd's of London) will be required to establish an equalisation provision after the Directive comes into force. This includes Solvency II firms and those that are currently out of Solvency II's scope. Out of scope firms will continue to be subject to the forward-looking Pillar 2 ICA when other firms become subject to Solvency II. These rules take account of the specific risks relating to the type of business written by these firms.
- 9.23** It may also be noted that Finance Bill 2012 repeals the legislation that allows general insurance companies to take a tax deduction for equalisation provisions as well as the repeal of parallel rules that apply to Lloyd's of London. The legislation will be repealed from the date the Directive comes into force. Transitional rules will apply for the taxation of any equalisation provisions still held at that time.

Cost benefit analysis

- 9.24** The proposal relating to the equalisation provision will reduce costs for firms since they will no longer need to calculate and set aside an equalisation provision. However, they will still be expected to assess the amount of capital they should hold taking account of the risks borne, so that the regulatory requirements will be better aligned with the risk profile of the firms, which should provide an economic benefit.

Q27: Do you agree that we should remove the current INSPRU 1.4 rules from the Handbook text and hence the requirement to maintain a claims equalisation provision for all GI firms?

GENPRU 2.1.38 ECR – Enhanced Capital Requirement

- 9.25** For general insurance firms in scope of Solvency I, we apply separately a 'soft' ECR test to assess the adequacy of their capital resources to cover underwriting and asset risks.
- 9.26** Our rules currently require GI firms to calculate an ECR through a series of factors that are applied to their premium income, technical provisions and asset values. These factors are intended to reflect the risks associated with different categories of GI business¹⁰ and different asset classes. The resulting ECR is reported to us each year through specific forms that are submitted alongside the annual returns, but the ECR is not shown in a public document. This ECR is a 'soft' test, since there is no requirement for firms to hold capital resources sufficient to cover the ECR.

¹⁰ The methodology for this component of the ECR is broadly similar to that applied for underwriting risks in the Solvency II SCR, but without the explicit application of correlation factors.

- 9.27 This ECR test then supplements the basic information provided to us in financial returns each year through the application of capital requirements (based on the current Solvency I Directive) that are less well attuned to the risks borne by insurers. While the latter capital requirements will remain in place for out of scope firms, we believe that we should therefore retain the ECR test for those out of scope firms to which the current rules apply, in order to provide for a better overall evaluation of GI business risks each year, and which also can be related where relevant to the firm's ICA/ICG.

Cost benefit analysis

- 9.28 The proposal relating to the ECR creates no incremental economic costs and benefits since we will maintain the status quo.

Q28: Do you agree that we should only apply the current rules relating to the calculation of an ECR to those GI firms to which these rules currently apply?

Currency denominations – GENPRU 2.1.30R, GENPRU 2.1.33R, INSPRU 1.1.45R, 1.1.47R, IPRU(INS) App 9.1, and IPRU(FSOC) Ch. 4

- 9.29 The current Solvency I directives for insurance and reinsurance firms include various amounts denominated in euros relating to the calculation of:
- the base capital resources requirement (BCRR) for insurance and reinsurance firms; and
 - the capital resources requirement (CRR) for firms writing general insurance business.
- 9.30 Similar amounts denominated in euros appear in our Handbook for both Solvency I firms and NDFs. These are then converted to UK sterling (and any other relevant reporting currencies) at the official rate of exchange at 31 October each year.
- 9.31 As most Solvency II out of scope firms write business denominated primarily in UK sterling, the calculation of the CRR and BCRR, and its equivalents (for NDFs), through the application of a variable exchange rate may cause disproportionate and unnecessary variations in their capital requirements and we propose converting the currency into sterling denominations for these firms, based on the euro amounts that will apply as at 31 December 2012 and an appropriate exchange rate. For this purpose, the draft instrument contains the corresponding proposed amendments to our rules, including up-to-date tables for the BCRR, and we propose to continue our current practice whereby these amounts may be increased from time to time, following consultation, to reflect underlying rates of inflation.

Cost benefit analysis

- 9.32 The proposal to convert euro amounts to sterling for the BCRR and CRR should not create large costs for firms and should accordingly benefit from less variations in capital requirements.

Q29: Do you agree that we should convert Euro amounts to sterling for the purpose of the calculation of the BCRR and CRR for out of scope firms?

Table showing proposed application of Handbook sections relevant to each category of insurance firm

Handbook section	UK Solvency II firms	Friendly societies out of scope of Solvency II	Other insurers out of scope of Solvency II	Incoming EEA firms	Incoming Treaty firms
SOLPRU	Y	N	N	N	N
INSPRU	N	N	Y	N	Y(Chapter 1.5 only)
GENPRU	Y (Chapter 3 only)	N	Y (other than Chapter 3)	N	N
IPRU(INS)	N	N	Y	N	N
IPRU(FSOC)	Y (Chapters 1, 2, 7 & 8 only)	Y	N	N	N
SUP	Y	Y	Y	Y	Y
SYSC	Y (Chapters 3, 12, and 18 only)	Y	Y	Y	Y
COND	Y	Y	Y	Y	Y
FIT	Y	Y	Y	Y	Y
COBS	Y	Y	Y	Y	Y
ICOBS	Y	Y	Y	Y	Y
PRIN	Y	Y	Y	Y	Y
GLOSSARY	Y	Y	Y	Y	Y

Notes

- 1) Some chapters or individual rules within each section of the Handbook may have a narrower scope of application than indicated by the general designations above.

- 2) The Society of Lloyd's and managing agents will be covered by relevant chapters of the sections of the Handbook that are applicable to Solvency II firms, although the relevant application provisions should be consulted for the specific application in each case.
- 3) The above table does not include non-EEA insurers, EEA-deposit insurers, or Swiss general insurers.
- 4) IPRU(FSOC) applies only to friendly societies, and not to other firms.

Q30: Do you agree with all of the consequential amendments?

Handbook guidance and Level 3 guidelines

- 9.33** As a general approach, guidance that occupies the same space as the Directive is to be switched off where we expect Level 3 guidelines will be forthcoming. Where existing guidance is retained, we expect to add cross-references to relevant SOLPRU rules where appropriate rather than moving or duplicating this material.

Annex 1

Diversity Impact Assessment

1. In line with its public sector duty under the Equality Act 2010, the FSA is required to consider the impact of any new rules or proposals on equality and diversity issues in the UK.
2. This Consultation Paper relates to the further transposition of the EU Solvency II Directive in the UK. In our first paper (CP11/22), we said that the implementation of this Directive is not expected to have any direct or indirect discriminatory impact under existing UK equality law. We maintain this view on the basis that the overall policy approach remains intact and unaffected by our latest proposals.
3. Thus none of the proposed rule changes in this CP are considered to raise issues of equality or diversity and to have any discriminatory impact in the UK.

Annex 2

Compatibility Statement

1. This Annex reaffirms our views on how the proposals to transpose the Solvency II Directive into UK law are compatible with our objectives and the principles of good regulation. This statement applies to the population of insurance firms covered by the Directive.

Compatibility with our statutory objectives

2. The further transposition of the Directive in our Handbook as set out in this CP aims to meet our statutory objectives, primarily our objective of consumer protection.

Consumer protection

3. Transposing Solvency II into UK law provides a significantly enhanced prudential regime with the key aim of providing greater policyholder protection.

Market confidence

4. Solvency II provides for a foundation of:
 - market-consistent valuation for assets and liabilities;
 - risk-sensitive capital requirements;
 - a requirement to apply stresses to both assets and liabilities;
 - a much stronger emphasis on risk management and forward-looking governance; and
 - greater market discipline through increased public disclosure.
5. This will give supervisors and markets greater clarity of firms' solvency positions and business models. The harmonised regime means this will now also apply across Europe.

This will enhance supervisors' and markets' understanding of the sector as a whole as well as of individual firms.

6. The requirements of Solvency II should also result in improved stress resilience and a reduced risk of firm failure. Ensuring the stability of UK insurance firms should maintain trust and confidence in UK insurance markets.

Financial stability

7. An enhanced and more resilient prudential regime will contribute towards greater financial stability to the advantage of consumers, investors and the insurance industry.

Reduction in financial crime

8. Solvency II is not directly aimed at reducing the incidence of financial crime.

Compatibility with the need to have regard to the principles of good regulation

9. Under Section 2 (3) of FSMA, we must consider the specific matters set out below, when carrying out our functions.

Efficiency and economy

10. Our aim is to transpose and implement this Directive in an efficient and economic manner giving as much clarity and certainty as possible based on:
 - 'intelligent copy-out' as far as possible, adhering to the wording of the Directive;
 - as closely as possible; and
 - optimal use and deployment of our own resources.

Role of management

11. The Directive places a significant role on senior management for ensuring compliance with the Directive together with an enhanced duty of public disclosure.

Principle that a burden or restriction should be proportionate to the benefits, considered in general terms, expected to result from imposing that burden or restriction

12. The Directive recognises that the new rules and requirements should not be too burdensome on small and medium-sized firms or on those providing specialist products to specific consumer groups. Having commissioned and reviewed an independent cost benefit analysis, the short-term costs of implementation have to be weighed against the longer-term qualitative benefits for firms.

Desirability of facilitating innovation in connection with regulated activities

13. By aligning capital requirements more closely with risks, Solvency II will encourage improvement in the insurance industry's risk management practices. This should improve the efficiency of capital allocation and facilitate innovation, both for risk management and product development.

International character of financial services and markets and the desirability of maintaining the competitive position of the UK

14. The Directive is aimed mainly at maximum harmonisation across Europe for insurers operating across different Member States. It also seeks to achieve consistent regulatory approaches and supervisory practices, and improved frequency and quality of disclosure.
15. In the areas where we have the option to make a discretionary decision, we have taken account of the competitive implications between firms based in the UK and in other countries.

Need to minimise the adverse effects on competition that may arise from anything done in the discharge of the FSA's functions

16. The cost benefit analysis undertaken indicates that the proposed changes resulting from transposition of Solvency II should not have material adverse effects on competition. We would welcome comments on this.

Desirability of facilitating competition between those who are subject to any form of regulation by us

17. Solvency II is designed to introduce more risk-sensitive capital requirements and promote effective risk management and governance across the insurance sector. This, in turn, should facilitate more effective competition across the wider financial sector.

Annex 3

List of Questions

Chapter 5 – Our approach to the Lloyd’s market

- Q1:** Do you have any views on whether, and if so, how we should replace our existing requirement in respect of the provision of statements of actuarial opinion?

Chapter 6 – Public disclosure of capital add-ons and USPs

- Q2:** Do you agree with our approach to exercising this option?

Chapter 7 – With profits insurance business

- Q3:** Do you agree with the changes that we have described above to the conduct rules for distributions?
- Q4:** Do you agree with our proposal to amend the definition of excess surplus for the purposes of the rule and evidential provision relating to the distribution of excess surplus?
- Q5:** Do you agree that for Solvency II firms we should disapply COBS 20.2.32R in relation to loans and produce new guidance as proposed?

- Q6:** Do you agree that we should retain this guidance as proposed, and introduce a new rule on support assets?
- Q7:** Do you agree to our retaining guidance on reviewing non-profit business, reinsurance and disclosure of decisions on strategic investments for all firms, but that for Solvency II firms that we disapply the rules and guidance referred to above which overlap the Prudent Person Principle?
- Q8:** Do you agree that we should introduce guidance to Solvency II firms writing with-profits business that the provisions implementing the Prudent Person Principle should be applied to the investment of with profits assets by reference to the particular circumstances within the with profits fund including in relation to strategic investments?
- Q9:** Do you agree that the changes to the provisions on ceasing to effect new business should be restricted to those required to align the rules with Solvency II terminology?
- Q10:** Do you agree with our proposals to amend the changes in surplus distribution notification requirements currently addressed by IPRU (INS) Chapter 3.3?
- Q11:** Do you agree that IPRU (INS) section 3.5 should be transcribed into COBS 20?
- Q12:** Do you agree that we should amend COBS 20.3 to require Solvency II firms who wish to use support assets to document and describe them in their PPFMs?
- Q13:** Do you agree that we should amend COBS 20.4.4 and that with-profits committees should also consider the existence and scope of sub-funds within COBS 20.5?

- Q14:** Do you agree that the proposed new provisions in COBS 20 relating to GENPRU 2.2.271R(1)-(3) are appropriate?
- Q15:** Do you agree that the governance and management provisions from INSPRU 1.5 should be converted into new rules in COBS 20 for Solvency II firms in order that policyholder interests continue to have adequate protection?
- Q16:** Do you agree that we should include a new rule in COBS 20 to require Solvency II firms to manage their with-profits fund to ensure that assets meet liabilities?
- Q17:** Do you agree with our proposals to amend definitions, as above, and to introduce a transitional provision (para 7.51)?
- Q18:** Do you agree that firms should be required to ask the court to review the appropriateness of their continued reliance on the transitional provision with the FSA when bringing a scheme back to court?
- Q19:** Do you agree with the proposed rules which specify the determination of assets shares, or equivalent calculations, in order to calculate approved surplus funds?
- Q20:** Do you agree with our revised definition of approved surplus funds and the proposed guidance on classification?

Chapter 8 – Unit-linked business

- Q21:** Do you agree with our proposals for the use of derivatives?
- Q22:** Do you agree with our proposal to amend COBS 21 to refer to the requirements of COLL 5.3 where funds using wider investment powers are offered to policyholders and beneficiaries who are natural persons and bear the direct investment risk?

- Q23:** Do you agree with our proposals on stock lending?
- Q24:** Do you agree that our proposals maintain the effect of the current level of protection in place in relation to stock lending for policyholders and beneficiaries?
- Q25:** Do you agree with our view that the Directive provides appropriate protection for unit-linked policyholders and beneficiaries?
- Q26:** Do you agree with the assessment of the appropriateness of the systems firms currently have in place? Do you agree that no further guidance is required?

Chapter 9 – Application of SOLPRU and Consequential amendments to Handbook

- Q27:** Do you agree that we should remove the current INSPRU 1.4 rules from the Handbook text and hence the requirement to maintain a claims equalisation provision for all GI firms?
- Q28:** Do you agree that we should only apply the current rules relating to the calculation of an ECR to those GI firms to which these rules currently apply?
- Q29:** Do you agree that we should convert Euro amounts to sterling for the purpose of the calculation of the BCRR and CRR for out of scope firms?
- Q30:** Do you agree with all of the consequential amendments?

Draft Handbook text

Appendix 1: Feedback to CP11/22 – SOLPRU

Appendix 2: Lloyd’s market

Appendix 3: Public disclosure: capital add-ons/undertaking specific parameters

Appendix 4: With-profits

Appendix 5: Unit-linked

Appendix 6: Consequential

Note:

1. The Appendices that follow setting out the proposed Handbook text are organised so that each Appendix contains the proposed Handbook text that corresponds to the subject of an individual Chapter of this CP. For example, Appendix 1: Feedback to CP 11/22 – SOLPRU sets out the proposed Handbook text discussed in CP 11/22 as is proposed to be amended following the consultation.
2. Each Appendix groups together all related Handbook text corresponding to the chapter. This helps the reader understand how the various parts of the Handbook text fit to deliver the policy covered in the chapter. So, for example, Appendix 4: With profits contains amendments to COBS 21 and SOLPRU, together with related Glossary amendments.
3. The FSA’s powers to make the proposed rules and guidance set out in the following Appendices are contained in the Financial Services and Markets Act 2000. The following sections in particular are relevant: section 138 (General rule-making power); section 141 (Insurance business rules); section 149 (Evidential provisions); section 150(2) (Actions for damages); section 156 (General supplementary powers); section 157(1) (Guidance); section 316 (Direction by Authority) and section 340 (Appointment of auditors and actuaries).

Appendix 1

Feedback to CP11/12 – SOLPRU

Annex A

Amendments to the Glossary of Definitions

Note to reader: The amendments proposed in this Annex are based on the versions of SOLPRU, Glossary and SUP 10 proposed in CP11/22 (Transposition of Solvency II).

In this Annex, underlining indicates new text and striking through indicates deleted text.

<i>ancillary own funds</i>	(1) (in relation to a <i>UK Solvency II firm</i> and the <i>Society</i>) <u>has the meaning given in SOLPRU 3.2.4R</u> and are the own funds determined in accordance with SOLPRU 3.2.4R to 3.2.10G; or
	...
<i>basic own funds</i>	(1) (in relation to a <i>UK Solvency II firm</i> and the <i>Society</i>), <u>has the meaning given in the own funds</u> determined in accordance with SOLPRU 3.2.2R; or
	...
<i>internal audit function</i>	controlled function CF15 in the table of controlled functions, described more fully in SUP 10.8.4R. [deleted]
<i>non-Solvency I firm</i>	a <i>firm</i> that immediately before the <i>Solvency II implementation date</i> was a non-directive firm <u>fell outside the scope of Solvency I Directive.</u>
<i>risk function</i>	controlled function CF14 in the table of controlled functions, described more fully in SUP 10.8.3R. [deleted]

Annex B

Prudential sourcebook for Solvency II Insurers (SOLPRU)

Note to reader: The amendments proposed in this Annex are based on the versions of SOLPRU, Glossary and SUP 10 proposed in CP11/22 (Transposition of Solvency II).

In this Annex, underlining indicates new text and striking through indicates deleted text.

3.2 Determination of own funds

3.2.1 R *A firm's own funds must* comprise the sum of its *basic own funds* and *ancillary own funds*.

[**Note:** article 87 of the *Solvency II Directive*]

3.2.2 R The *firm's basic own funds must* consist of the following items:

...

...

3.2.4 R Subject to SOLPRU 3.2.6R, the ~~The~~ *firm's ancillary own funds must,* ~~subject to SOLPRU 3.2.6R,~~ consist of items (other than items of *basic own funds*) which can be called up to absorb losses, including the following (to the extent that they are not items of *basic own funds*):

...

...

11 Group supervision

...

11.2 Levels

11.2.1 R If the *participating Solvency II undertaking* or the *insurance holding company* referred to in SOLPRU 11.1.2R(1) or (2) (~~instances of group supervision~~) is itself a *subsidiary undertaking* of another *Solvency II undertaking* or of another *insurance holding company* which has its head office in an *EEA State*, then SOLPRU 11.3 to SOLPRU 11.9 (Group solvency) applies only at the level of the *ultimate EEA insurance parent undertaking*.

[**Note:** article 215(1) of the *Solvency II Directive*]

11.2.2 R If the *FSA* makes the decision referred to in article 216(1) of the *Solvency II Directive* (group supervision at national level) then SOLPRU 11.3 to SOLPRU 11.9 (Group solvency) apply with any necessary changes, subject

to articles 216(6) and 217 of the *Solvency II Directive* and the following:

- (1) if the *FSA* so determines, group supervision of the *ultimate UK Solvency II insurance parent undertaking* at national level is restricted to those sections of *SOLPRU 11.3* to *SOLPRU 11.9* (other than *SOLPRU 11.9.5G*) that the *FSA* specifies; and

...

11.3 Group solvency: general provisions

- 11.3.1 R Where *SOLPRU 11.1.2R(1)(a)* (~~instances of group supervision~~) applies, each *participating Solvency II undertaking* in the *insurance group* must ensure that *eligible own funds* are available in the *insurance group* which are always at least equal to the *group SCR* as calculated in accordance with *SOLPRU 11.4* to *SOLPRU 11.5*.

[**Note:** article 218(2) of the *Solvency II Directive*]

- 11.3.2 R Where *SOLPRU 11.1.2R(2)* (~~instances of group supervision~~) applies, each *Solvency II undertaking* in the *insurance group* must ensure that *eligible own funds* are available in the *insurance group* which are always at least equal to the *group SCR* as calculated in accordance with *SOLPRU 11.6*.

[**Note:** article 218(3) of the *Solvency II Directive*]

- 11.3.3 R *Relevant insurance group undertakings* must have procedures in place to identify deteriorating financial conditions within the *insurance groups* of which they are members and must immediately notify the *FSA group supervisor* when that deterioration occurs.

[**Note:** articles 218(4) and 136 of the *Solvency II Directive*]

...

- 11.3.5 R *Relevant insurance group undertakings* must:

...

- (3) take the measures determined by the *FSA* to achieve, within six *months* (or such longer period as the *FSA* may determine, in accordance with *SOLPRU 6.3.2G*) from the observation of non-compliance with the *group SCR*, the re-establishment of the level of *eligible own funds* covering the *group SCR* or the reduction of the risk profile to ensure compliance with the *group SCR*; and

...

...

11.4 Group solvency: choice of calculation method and basic principles

- 11.4.1 R The calculation of the solvency at the level of the *insurance group* of the *Solvency II undertakings* referred to in SOLPRU 11.1.2R(1) (~~instances of group supervision~~) must be carried out:

...

...

Elimination of double use of eligible own funds

- 11.4.5 R *Own funds eligible for the SCR* must not be taken into account more than once among the different *Solvency II undertakings* taken into account in the calculation of the solvency of an *insurance group*. For that purpose, when calculating the solvency of an *insurance group* and where *method 1* and *method 2* do not provide for it, the following amounts must be excluded:

...

- (2) the value of any asset of a *related Solvency II undertaking* of the *participating Solvency II ~~undertakings~~ undertaking* which represents the financing of *own funds eligible for the SCR* of that *participating Solvency II ~~undertakings~~ undertaking*; and

...

...

11.5 Calculation methods

Method 2

- 11.5.5 R The group solvency of the *participating Solvency II undertaking* in an *insurance group* is the difference between the following:

...

- (2) the value in the *participating Solvency II undertaking* of the *related Solvency II ~~undertaking~~ undertakings* and the aggregated *group SCR*, as provided for in SOLPRU 11.5.7R.

...

...

11.7 Groups with centralised risk management

- 11.7.1 R SOLPRU 11.7.3R applies to any *Solvency II undertaking* in an *insurance group* which is a *subsidiary undertaking* of another *Solvency II undertaking* or of an *insurance holding company* where all of the following conditions are satisfied:

...

- (3) ~~the *parent undertaking* is or one or more *relevant insurance group undertaking* that is permitted, under SOLPRU 11.9.2R(3) (group ORSA), to produce a single document covering all relevant ORSAs;~~

(a) the *parent undertaking*; or

(b) one or more *relevant insurance group undertakings*,

is permitted, under SOLPRU 11.9.2R(3) (group ORSA), to produce a single document covering all relevant ORSAs;

- (4) ~~the *parent undertaking* is or one or more *relevant insurance group undertaking* that is permitted, under SOLPRU 11.9.4R(2) (group SFCR), to produce a single SFCR covering all relevant *Solvency II undertakings* and *insurance holding companies*; and;~~

(a) the *parent undertaking*; or

(b) one or more *relevant insurance group undertaking*,

is permitted, under SOLPRU 11.9.4R(2) (group SFCR), to produce a single SFCR covering all relevant *Solvency II undertakings* and *insurance holding companies*; and

...

...

11.8 Risk concentration and intra-group transactions

11.8.1 R (1) ...

- (2) The necessary information must be submitted to the *group supervisor* by the *Solvency II undertaking* which is at the head of the *insurance group* or, where the *insurance group* is not headed by a *Solvency II undertaking*, by such other *Solvency II undertaking* in the *insurance group* as the *group supervisor* may specify.

[Note: article 244 of the *Solvency II Directive*]

11.8.2 R ...

- (3) The necessary information must be submitted to the *group supervisor* by the *Solvency II undertaking* which is at the head of the *insurance group* or, where the *insurance group* is not headed by a *Solvency II undertaking*, by such other *Solvency II undertaking* in the *insurance group* as the *group supervisor* may specify.

[Note: article 245 of the *Solvency II Directive*]

...

11.10 Third countries

- 11.10.1 R When calculating the solvency of an *insurance group* falling within SOLPRU 11.1.2R(3) (~~instances of group supervision~~), the *parent undertaking* (being an *insurance holding company* which does not have its head office in an *EEA State* or a *third country insurance undertaking* or a *third country reinsurance undertaking*) must, solely for the purposes of that calculation, be treated as a ~~related Solvency II undertaking~~ UK Solvency II firm to which SOLPRU 11.1.2R(1)(a) applies unless:

...

- 11.10.2 R Where the *parent undertaking* referred to in SOLPRU 11.1.2R(3) (~~instances of group supervision~~) is itself a *subsidiary undertaking* of an *insurance holding company* which does not have its head office in an *EEA State* or a *third country insurance undertaking* or a *third country reinsurance undertaking*, SOLPRU 11.10.1R applies at the level of either:

...

11.11 Mixed-activity insurance holding companies

- 11.11.1 R SOLPRU 11.8.2R (supervision of intra-group transactions) applies, with any necessary changes, to *insurance groups* falling within SOLPRU ~~11.1.2R(3)~~ (~~instances of group supervision~~) 11.1.2R(4).

[Note: article 265 of the *Solvency II Directive*]

12 Reporting

...

12.3 Public disclosure – solvency and financial condition report

...

- 12.3.5 R The disclosure required by SOLPRU 12.3.3R(5)(b) must include the following:
- (1) the amount of the *SCR* calculated by the *firm* using the *standard formula* ~~and~~ or, where the *firm* has received *internal model approval*, the amount of the *SCR* calculated using its *internal model* ~~and~~, where applicable in the case of a partial *internal model*, the *standard formula*;

...

Annex C

Amendments to the Supervision manual (SUP)

Note to reader: The amendments proposed in this Annex are based on the versions of SOLPRU, Glossary and SUP 10 proposed in CP11/22 (Transposition of Solvency II). Changes to the Handbook that were proposed in CP11/22 retained underlining in the text in this Annex, and then subsequent changes proposed to that version in CP11/22 as contained within this Annex.

In this Annex, underlining indicates new text and striking through indicates deleted text.

10 Approved Persons

...

10.4 Specification of functions

...

10.4.5 R Controlled functions

Type	CF	Description of controlled function
------	----	------------------------------------

...

<i>Required functions*</i>	...
----------------------------	-----

<i>Systems Group of systems and controls function functions*</i>	...
---	-----

28	<i>Systems and controls function</i>
----	--------------------------------------

14	<u><i>Risk function</i></u>
----	-----------------------------

15	<u><i>Internal audit function</i></u>
----	---------------------------------------

[deleted]

...

...

10.8 Systems ~~Group of systems~~ and controls functions

Systems and controls functions (CF28)

10.8.1 R ~~The~~ For a firm that is not a UK Solvency II firm the Society or a managing agent, the systems and controls function is the function of acting in the

capacity of an *employee* of the *firm* ~~that is not a UK Solvency II firm~~ with responsibility for reporting to the *governing body* of a *firm*, or the audit committee (or its equivalent) in relation to:

...

10.8.1A R For a UK Solvency II firm, the Society and managing agents, the systems and controls function is the function of acting in the capacity of an employee with responsibility for either:

- (1) reporting to the governing body of a firm, or the audit committee (or its equivalent) in relation to its financial affairs;
- (2) the risk management function set out in SOLPRU 9.3.3R; or
- (3) the internal audit function set out in SOLPRU 9.5.1R.

10.8.1B G SOLPRU 9.5.1R(2) requires the internal audit function of a UK Solvency II firm to be independent from the operational functions. The operational functions include the risk management function set out in SOLPRU 9.3.3R. The FSA would therefore expect a UK Solvency II firm, the Society and managing agents to have at least two employees approved for the systems and controls function.

10.8.1C R A UK Solvency II firm, the Society and managing agents must notify the FSA if the role of an employee performing the systems and controls function set out in SUP 10.8.1AR(1), (2) or (3) changes such that the employee is performing some other role set out in SUP 10.8.1AR.

10.8.1D G Following a notification received pursuant to SUP 10.8.1CR, the FSA may, in accordance with FIT, consider the continuing fitness and propriety of that employee to perform the systems and controls function, taking into account the change to the employee's role.

...

10.8.2A G ...

10.8.2B G ~~If:~~

- (1) ~~a UK Solvency II firm chooses to appoint an employee with responsibility for reporting to the governing body of the firm in relation to its financial affairs; and~~
- (2) ~~by carrying out that part of the systems and controls function, that employee will be effectively running the firm or will be responsible for some other key function;~~

~~the obligations on the firm to assess fitness and propriety in accordance with SOLPRU 9.8 (Fit and proper requirements) will apply and such employee is likely to be performing at least one other controlled function that is~~

applicable to a UK Solvency II firm. [deleted]

The risk function (CF14)

- 10.8.3 R The *risk function* is the function of acting in the capacity of an *employee* who is responsible for the risk management *function* set out in SOLPRU 9.3.3R. [deleted]

The internal audit function (CF15)

- 10.8.4 R The *internal audit function* is the function of acting in the capacity of an *employee* who is responsible for the internal audit *function* set out in SOLPRU 9.5.1R. [deleted]

...

Appendix 2

Our approach to the Lloyd's market

Annex A

Amendments to the Prudential sourcebook for Solvency II Insurers (SOLPRU)

In this Annex all text follows chronologically from the text proposed for the new *SOLPRU* sourcebook within CP11/22.

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

2 Valuation

Application

- 2.1.1 R ...
- 2.1.2 R *SOLPRU 2.2 (Valuation of assets and liabilities) applies to:*
- (1) *the Society* in accordance with *SOLPRU 13.2.1R*; and
- (2) *managing agents* in accordance with *SOLPRU 13.2.2R*.
- 2.1.3 R *SOLPRU 2.3 (Rules relating to technical provisions) and SOLPRU 2.4 (Calculation of technical provisions) apply to:*
- (1) *the Society* in accordance with *SOLPRU 13.2.1R*; and
- (2) *managing agents* in accordance with *SOLPRU 13.2.2R*,
- as modified by the provisions of *SOLPRU 2.5*.
- ...

The following is new text and is not underlined.

2.5 Valuation: Lloyd's

- 2.5.1 R *SOLPRU 2.5* applies to the *Society* and *managing agents*.
- 2.5.2 G For the purpose of complying with *SOLPRU 2.1.3R(1)*, the *Society* must calculate *technical provisions* in respect of the *insurance business* of each *member*.
- 2.5.3 G *SOLPRU 2.5.2G* recognises that *members* may participate on multiple *syndicates* which are not all managed by the same *managing agent*.
- 2.5.4 G For the purpose of complying with *SOLPRU 2.1.3R(2)*, a *managing agent* must calculate *technical provisions* in respect of each *syndicate* it manages.

- 2.5.5 R In respect of business that has been subject to an *approved reinsurance to close, managing agents* must calculate *technical provisions* (before and after deduction of reinsurance cessions) for the reinsuring and not for the reinsured *member*.

The risk margin

- 2.5.6 G For the purposes of *SOLPRU 2.4.5R* in relation to *managing agents*, the reference to “SCR” in *SOLPRU 2.4.5R* is to be construed as a reference to the notional *syndicate SCR* required to be calculated pursuant to *SOLPRU 4.32* (Syndicate notional SCR and member notional SCR).

Segmentation

- 2.5.7 R For the purposes of *SOLPRU 2.4.10R* in relation to *managing agents*, a *managing agent* must carry out the segmentation referred to in that *rule* in respect of each *syndicate* managed by the *managing agent*.

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

3 Own funds

3.1 Application

- 3.1.1 R ...

- 3.1.2 R *SOLPRU 3.2 (Determination of own funds) and SOLPRU 3.3 (Classification and eligibility of own funds) apply to the Society in accordance with SOLPRU 13.2.1R, as modified by the provisions of SOLPRU 3.4.*

...

The following is new text and is not underlined.

3.4 Own funds: Lloyd’s

Application

- 3.4.1 R *SOLPRU 3.4* applies to the *Society*.

Determination of own funds

- 3.4.2 G In determining *own funds* at Lloyd’s in accordance with *SOLPRU 3.2*, the *Society* may have regard to:

- (1) the *Society’s central assets* and *central liabilities*; and

- (2) the assets and liabilities of *members*, including assets which are available to support *members' insurance business* at Lloyd's, such assets including a *member's funds at Lloyd's*.
- 3.4.3 G Items at Lloyd's from which *own funds* will be determined and classified will come from a number of different sources, including the *Society's central assets* and *central liabilities*, and the assets and liabilities of *members*. For the purposes of SOLPRU 4 (Solvency capital requirement), as applied to the *Society* and *managing agents*, it will be necessary for the *Society* to determine the provenance of *own fund* items as between the *Society* and *members*.

Classification and eligibility of own funds

- 3.4.4 R The *Society* must categorise *own funds* at Lloyd's as between:
- (1) *own funds* attributable to the *Society*; and
- (2) *own funds* attributable to *members* which are available to support *members' insurance business* at Lloyd's, including *funds at Lloyd's*.
- 3.4.5 G SOLPRU 3.3.1G provides that *own funds* which are classified as *Tier 1 own funds* can be used to cover a firm's *MCR* and *SCR* without limit. Other items of *own funds* are only eligible to cover the *SCR* (including the *central requirement*) and *MCR* subject to limits. SOLPRU 4.30.2R requires the *Society* to ensure that *eligible own funds* are held at Lloyd's covering its *SCR*. SOLPRU 4.30 contains additional provisions concerning how the Lloyd's *SCR* is to be covered with *eligible own funds*.

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

4 Solvency capital requirement

General

4.1 Application

- 4.1.1 R ...
- 4.1.2 R SOLPRU 4.2 (Requirement to hold own funds covering the SCR) to SOLPRU 4.28 (Capital add-on) apply to the Society in accordance with SOLPRU 13.2.1R, as modified by the provisions of SOLPRU 4.29 to SOLPRU 4.36.
- 4.1.3 G SOLPRU 4.32 also applies to a managing agent.

...

The following is new text and is not underlined.

4.29 Solvency capital requirement: Lloyd's

Application generally of SOLPRU 4.30 to SOLPRU 4.36

- 4.29.1 G *SOLPRU 4.29 to SOLPRU 4.35* modifies the application of *SOLPRU 4* as to how the *SCR* is to be calculated at Lloyd's. *SOLPRU 4.36* describes how a *capital add-on* will apply at Lloyd's should it be imposed. With the exception of *SOLPRU 4.32*, these requirements apply to the *Society*. Each section contains a *rule* specifying its precise application.

4.30 Requirement to hold eligible own funds covering the SCR

- 4.30.1 R *SOLPRU 4.30* applies to the *Society*.
- 4.30.2 R The *Society* must ensure that *eligible own funds* are held at Lloyd's covering its *SCR*.
- 4.30.3 G *SOLPRU 4.31 to SOLPRU 4.33* contain requirements which are relevant to calculating the *SCR* at Lloyd's. *SOLPRU 4.34* and *SOLPRU 4.35* contain further provisions which apply depending upon whether the *SCR* at Lloyd's will be calculated using the *standard formula* or an *internal model*. The *SCR* at Lloyd's includes a *central requirement* which takes account of risks to the *Society*.

SCR: central requirement

- 4.30.4 R *Eligible own funds* covering the *central requirement* must be *eligible own funds* attributable to the *Society*.
- 4.30.5 G The requirement to hold *eligible own funds* covering the *central requirement* is intended to ensure that risks to the *Society*, including risks to *central assets* (including the risk that *own funds* attributable to a *member* may not be sufficient to enable the *member* to meet obligations arising from the *member's insurance business* at Lloyd's) are suitably covered by the *Society*.

SCR: standard formula

- 4.30.6 R Where the *standard formula* is used by the *Society* to calculate the *SCR* for Lloyd's, the *Society* must carry out the following process before it will be taken to have demonstrated that *SOLPRU 4.30.2R* is met:
- (1) *own funds* attributable to a *member* are to be compared with the *member's* notional *SCR* derived pursuant to *SOLPRU 4.32.5R*;
 - (2) where the *own funds* attributable to the *member* are less than or equal to that *member's* notional *SCR*, such *own funds* (but no additional

own funds attributable to that *member*, including any *own funds* which are greater than the *member's* notional *SCR*) are to be taken into account for the purposes of establishing compliance with *SOLPRU* 4.30.2R; and

- (3) to the extent the *own funds* attributable to the *member* are less than that *member's* notional *SCR* derived pursuant to *SOLPRU* 4.32.5R, the *Society* must hold *own funds* in respect of the difference.

SCR: internal model

- 4.30.7 R Where the *Society* uses an approved *internal model*, the *Society* must also ensure that *eligible own funds* are held at Lloyd's covering, for at least 99.5% of the scenarios taken into account in the *internal model* for the purposes of meeting *SOLPRU* 4.3.4R, any diminution in *own funds* at Lloyd's arising from the impact of those scenarios.
- 4.30.8 R Where an approved *internal model* is used by the *Society* to calculate the *SCR*, for the purpose of meeting the requirement set out in *SOLPRU* 4.30.2R, the *Society* may take account of *own funds* attributable to a *member* only to the extent of the diminution, if any, to those *own funds* resulting from the application of risk scenarios taken into account in the *internal model*.
- 4.30.9 G *SOLPRU* 4.30.8R recognises that *own funds* attributable to a *member* are not available to absorb the losses of other *members*, or any losses of the *Society*. Consequently, in respect of *own funds* attributable to a *member*, where there is no diminution in those *own funds* consequent upon the application of scenarios taken into account in the *internal model*, those *own funds* attributable to that *member* must not be taken into account for the purposes of satisfying *SOLPRU* 4.30.2R. Similarly, in respect of *own funds* attributable to a *member*, any surplus of *own funds* in excess of the diminution to those *own funds* consequent upon the application of the scenarios taken account of in the *internal model*, must not be taken into account for the purposes of satisfying *SOLPRU* 4.30.2R.

4.31 General provision for the calculation of the SCR: Lloyd's

- 4.31.1 R *SOLPRU* 4.31 applies to the *Society*.
- 4.31.2 R In calculating the *SCR* for Lloyd's, the *Society* must ensure that the *SCR* is calibrated so as to include all quantifiable risks to which:
- (1) *members* are exposed as a consequence of those *members* carrying on *insurance business* at Lloyd's; and
 - (2) the *Society* is exposed, including risks to the *central assets* and *central liabilities*,

in the manner required by *SOLPRU* 4.3 (General provisions for the calculation of the SCR) and, where an *internal model* is used, in accordance with *SOLPRU* 4.12.1R(2).

4.32 Syndicate notional SCR and member notional SCR

Syndicate notional SCR

- 4.32.1 R *SOLPRU* 4.32 applies to *managing agents* and, where specified, the *Society*.
- 4.32.2 R A *managing agent* must calculate a notional *SCR* for each *syndicate* which it manages.
- 4.32.3 R The notional *SCR* for each *syndicate* referred to in *SOLPRU* 4.32.2R must be calculated using a methodology which is consistent with the method used by the *Society* to derive the *SCR* for Lloyd's.
- 4.32.4 G The notional *syndicate SCR* will assist the *Society* in determining the notional *SCR* of each *member* of the *syndicate* pursuant to *SOLPRU* 4.32.5R. However, the notional *member SCR* will, to the extent applicable, also take account of diversification effects in respect of *members* participating on more than one *syndicate* which have not been reflected in the notional *syndicate SCR*.

Member notional SCR

- 4.32.5 R The *Society* must calculate a notional *SCR* for each *member* using the method of calculation chosen to calculate the *SCR* for Lloyd's for the purpose of *SOLPRU* 4.3.1R.

General duty upon managing agents to assist the Society

- 4.32.6 R Where a *managing agent* manages risks which are included in the Lloyd's *SCR* calculation, the *managing agent* must promptly assist and provide all relevant information to the *Society* for the purposes of the *Society* complying with *SOLPRU* 4 (Solvency capital requirement).

4.33 Central requirement

- 4.33.1 R *SOLPRU* 4.33 applies to the *Society*.
- 4.33.2 R The *Society* must calculate a *central requirement* for Lloyd's which meets *SOLPRU* 4.31.2R(2).
- 4.33.3 R The *central requirement* must take account of the risk that the *central assets* may be used to meet deficiencies (as to amount or quality) in *own funds* attributable to *members*, such *own funds* supporting *members' insurance*

business at Lloyd's.

4.34 Standard formula: Lloyd's

- 4.34.1 R *SOLPRU* 4.34 applies to the *Society* in relation to the use of the *standard formula* for the purpose of *SOLPRU* 4.3.1R.
- 4.34.2 R The *Society* must aggregate the results of each notional *SCR* referred to in *SOLPRU* 4.32.5R together with the *central requirement*, in order to obtain the *SCR* for Lloyd's.

4.35 Internal models: Lloyd's

- 4.35.1 R *SOLPRU* 4.35 applies to the *Society* in relation to the use of an *internal model* for the purpose of *SOLPRU* 4.3.1R.
- 4.35.2 R The *internal model* must:
- (1) separately identify and aggregate any diminution in *basic own funds* arising as a result of the application of risk scenarios taken into account in the *internal model* to:
 - (a) the *insurance business* of members; and
 - (b) the *central assets* and *central liabilities*; and
 - (2) where the risk scenarios taken into account in the *internal model* result in the *own funds* attributable to a particular *member* being exhausted, identify the consequent impact upon *own funds* attributable to the *Society*.
- 4.35.3 G The approach set out in *SOLPRU* 4.35.2R is, when combined with the *internal model* requirements set out in *SOLPRU* 4.21 to *SOLPRU* 4.27 and *SOLPRU* 4.31.2R, intended to produce, for each risk taken into account in the *internal model*, the negative impact on *basic own funds* at Lloyd's. In this way, the effect of the application of the risks taken into account in the *internal model* may be determined in respect of Lloyd's as a whole.

4.36 Capital add-on: Lloyd's

- 4.36.1 R *SOLPRU* 4.36 (Capital add-on: Lloyd's) applies to the *Society*.
- 4.36.2 G *SOLPRU* 4.33.2R requires the *Society* to calculate a *central requirement* for Lloyd's. As the *central requirement* forms part of the Lloyd's *SCR*, the provisions of article 37 of the *Solvency II Directive* will apply to any risk profile deviation on the part of the *Society* from the assumptions underlying

the calculation of the *central requirement*. As noted in SOLPRU 4.28.2G, the FSA will exercise the power to apply a *capital add-on* under the Act.

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

5 Minimum capital requirement

5.1 Application

5.1.1 R ...

5.1.2 R SOLPRU 5.2 (General provisions) to SOLPRU 5.4 (Frequency and reporting in relation to MCR) applies to the Society in accordance with SOLPRU 13.2.1R, as modified by SOLPRU 5.5.

...

The following is new text and is not underlined.

5.5 Minimum capital requirement: Lloyd's

Application

5.5.1 R SOLPRU 5.5 applies to the Society.

Calculation of the MCR

5.5.2 R In calculating the MCR for Lloyd's, as required by SOLPRU 5.3 (Calculation of the MCR), the Society must include risks arising as a consequence of *members* carrying on *insurance business* at Lloyd's, together with any risks to the Society, including risks to the *central assets* and *central liabilities*.

Determination of reporting points

5.5.3 R The Society must determine, at least quarterly, the ratio of the Lloyd's MCR to the Lloyd's SCR and notify the FSA of the result at the same time it reports the quarterly MCR calculation required by SOLPRU 5.4.1R.

5.5.4 R The Society must calculate a reporting point for each *underwriting member*, in accordance with SOLPRU 5.5.5R.

5.5.5 R The reporting point for each *underwriting member* must be calculated using the ratio referred to in SOLPRU 5.5.3R, expressed as a percentage, of the *member's* notional SCR referred to in SOLPRU 4.32.5R.

Notification of own funds falling below reporting point

- 5.5.6 R The *Society* must notify the *FSA* if *own funds* attributable to a *member* fall below the reporting point determined in accordance with *SOLPRU 5.5.5R* as soon as it is observed by the *Society*.

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

6 Insurance and reinsurance undertakings in difficulty or in an irregular situation

6.1 Application

6.1.1 R ...

6.1.2 R *SOLPRU 6.2 (Identification and notification of deteriorating financial conditions) to SOLPRU 6.6 (Transitional arrangements regarding compliance with the MCR) applies to the Society in accordance with SOLPRU 13.2.1R, as modified by the provisions of SOLPRU 6.7.*

...

The following is new text and is not underlined.

6.7 Insurance and reinsurance undertakings in difficulty or in an irregular situation: Lloyd's

Application

6.7.1 R *SOLPRU 6.7* applies to the *Society*.

6.7.2 G *SOLPRU 6.3 (Non-compliance with the SCR) and SOLPRU 6.5 (Recovery plan and finance scheme) apply to the Society such that a breach of the central requirement will be treated as a breach of the SCR.*

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

7 Investments

7.1 Application

7.1.1 R ...

7.1.2 R *SOLPRU 7.2 (Prudent person investment principle) applies to:*

(1) the Society in accordance with SOLPRU 13.2.1R; and

(2) managing agents in accordance with SOLPRU 13.2.2R.

...

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

8 Composites

8.1 Application

...

8.1.3 R Except as specified in SOLPRU 8.1.4R, SOLPRU 8.2 (Pursuit of life and non-life activity) to SOLPRU 8.5 (Links between general insurers and long-term insurers) applies to:

(1) the Society in accordance with SOLPRU 13.2.1R; and

(2) managing agents in accordance with SOLPRU 13.2.2R.

as modified by the requirements of SOLPRU 8.6.

8.1.4 R SOLPRU 8.2 (Pursuit of life and non-life activity) to SOLPRU 8.4 (Minimum financial obligations) do not apply to a managing agent which manages one or more syndicates, all of which carry out exclusively reinsurance.

...

The following is new text and is not underlined.

8.6 Composites: Lloyd's

Application

8.6.1 R SOLPRU 8.6 applies to the *Society* and *managing agents*.

Pursuit of life and non-life activity at Lloyd's: interpretation

8.6.2 G As Lloyd's is (and was prior to 15 March 1979, being the relevant date set out in the *Solvency II Directive*) composed of *syndicates* which separately accept *general insurance business* or *long-term insurance business*, the FSA considers Lloyd's to be a composite undertaking for the purposes of the *Solvency II Directive*. The *Solvency II Directive* requires *composite firms* to maintain separate management of *general insurance business* and *long-term insurance business*. In practical terms, this requires that *managing agents* separately manage *syndicates* which carry on *general insurance business* from *syndicates* which carry on *long-term insurance business*. However, where a single *syndicate* carries on both *general insurance business* and

long-term insurance business pursuant to the exceptions referred to at SOLPRU 8.2.3G, the FSA expects *managing agents* to apply the requirements of SOLPRU 8 (Composites) as modified by SOLPRU 8.6. The *guidance* set out in SOLPRU 8.6.3G and SOLPRU 8.6.4G is intended to assist in determining when the requirements of SOLPRU 8 will apply to *managing agents*.

- 8.6.3 G SOLPRU 8.2 (Pursuit of life and non-life activity) refers to a *firm's* permission to effect or carry out contracts of insurance which may be *general insurance business* or *long-term insurance business*, or both, and, within those categories, to the particular *classes* of *insurance business*. For the purpose of the application of SOLPRU 8 (Composites) to Lloyd's, references in SOLPRU 8.2 (Pursuit of life and non-life activity) to a *firm's* "permission" in respect of "classes" of *insurance business* are to be interpreted by reference to *syndicates* which carry out what would be:
- (1) *general insurance business*, if the *syndicate* was a *firm* authorised to effect and carry out contracts of *general insurance business*;
 - (2) *long-term insurance business*, if the *syndicate* was a *firm* authorised to effect and carry out contracts of *long-term insurance business*; and
 - (3) both *general insurance business* and *long-term insurance business*, if the *syndicate* was a *firm* authorised to effect and carry out both contracts of *general insurance business* and contracts of *long-term insurance business*, as contemplated by SOLPRU 8.2.3G,

as the context so requires, and references in SOLPRU 8.3 (Long-term and general insurance activities to be separately managed) to "general insurance business" and "long-term insurance business," and the activities relating thereto, are to be similarly interpreted.

- 8.6.4 G If SOLPRU 8.2 (Pursuit of life and non-life activity) to SOLPRU 8.4 (Minimum financial obligations) applies to a *managing agent* as specified in SOLPRU 8.6, it will apply to the *managing agent* in one or both of the following situations:
- (1) in respect of a *syndicate* managed by the *managing agent* which, having regard to SOLPRU 8.6.3G, carries out both *long-term insurance business* and *general insurance business* in accordance with the exceptions referred to at SOLPRU 8.2.3G; and
 - (2) which manages more than one *syndicate* in circumstances where those *syndicates*, having regard to SOLPRU 8.6.4G, do not exclusively carry on either *long-term insurance business* or *general insurance business*.

General insurance business and long-term insurance business carried on in one syndicate

- 8.6.5 R Other than as permitted by *SOLPRU 8*, a *managing agent* must not permit both *general insurance business* and *long-term insurance business* to be carried on together through any *syndicate* managed by it.

Application of *SOLPRU 8.4* (Minimum financial obligations)

- 8.6.6 R *SOLPRU 8.4.6R* to *SOLPRU 8.4.18G* do not apply to *managing agents*.

Other provisions relevant to business carried on at Lloyd's

- 8.6.7 R The *Society* and *managing agents* must take all reasonable steps to ensure that:
- (1) a *corporate member* does not carry on any commercial business other than *insurance business* and activities arising directly from that business; and
 - (2) *individual members* do not, in their capacity as *underwriting members*, carry on any commercial business other than *insurance business* and activities arising directly from that business.

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

9 Conditions governing business

9.1 Application

- 9.1.1 R ...

- 9.1.2 R *SOLPRU 9.2* (General governance requirements) to *SOLPRU 9.12* (Premiums for new business) applies to:

- (1) the *Society* in accordance with *SOLPRU 13.2.1R*; and
- (2) *managing agents* in accordance with *SOLPRU 13.2.2R*,
as modified by the requirements of *SOLPRU 9.13*.

...

The following is new text and is not underlined.

9.13 Conditions governing business: Lloyd's

Application

- 9.13.1 R *SOLPRU 9.13 applies to the Society and managing agents.*
- 9.13.2 G The *Society and managing agents* are required to separately apply the requirements of *SOLPRU 9* (Conditions governing business), although the manner in which those requirements are applied will differ as between the *Society and managing agents*, particularly where a *managing agent* manages more than one *syndicate*. The *FSA* considers that, usually, a *managing agent* will not be required to separately establish the *functions* required by *SOLPRU 9* (Conditions governing business) in respect of each *syndicate* managed by it.

Risk management

- 9.13.3 G For the purposes of *SOLPRU 9.3.1R(2)(b)*, as applied to *managing agents*, the reference to “SCR” in that rule is to be interpreted as a reference to the notional *syndicate SCR* required to be calculated by a *managing agent* in *SOLPRU 4.32.2R*.
- 9.13.4 G For the purpose of *SOLPRU 9.3.4R*, as applied to *managing agents*, the reference to “internal model” in that rule is to be interpreted as a reference to any *internal model* utilised by a *managing agent* to calculate the notional *syndicate SCR* pursuant to *SOLPRU 4.32.2R*.

Own risk and solvency assessment (ORSA)

- 9.13.5 R For the purpose of *SOLPRU 9.3.5R*, as applied to *managing agents*:
- (1) *managing agents* must conduct an *ORSA* for each *syndicate* which they manage;
 - (2) the reference to “capital requirements” in *SOLPRU 9.3.5R(2)(b)(i)* is to be interpreted as a reference to the notional *syndicate SCR* calculated by *managing agents* in *SOLPRU 4.32.2R*;
 - (3) the reference to “standard formula” and “internal model” in *SOLPRU 9.3.5R(2)(c)* is to be interpreted as a reference to the method of calculating the notional *syndicate SCR* referred to in *SOLPRU 4.32.2R*;
 - (4) the reference to “internal model” in *SOLPRU 9.3.5R(4)* is to be interpreted as a reference to any *internal model* used by a *managing agent* to calculate the notional *syndicate SCR* as required by *SOLPRU 4.32.2R*;
 - (5) the reference to “risk profile” in *SOLPRU 9.3.7R* is to be interpreted as a reference to the risk profile of any *syndicate* managed by the *managing agent*; and
 - (6) [Placeholder for reporting requirement referred to in *SOLPRU 9.3.8R* but not being consulted on in this consultation paper.]

Actuarial function

- 9.13.6 R For the purposes of *SOLPRU* 9.6.1R(1)(i), as applied to *managing agents*, the reference to “capital requirements” is to be interpreted as a reference to the notional *syndicate SCR* calculated by *managing agents* in *SOLPRU* 4.32.2R.

Fit and proper requirements for persons who effectively run the undertaking or have other key functions

- 9.13.7 G *SOLPRU* 9.8 (Fit and proper requirements for persons who effectively run the undertaking or have other key functions) applies to *managing agents* and the *Society*.

Functions to be established by the Society and managing agents

- 9.13.8 R Where a provision of *SOLPRU* 9 (Conditions governing business) requires that a *function* be established, the *Society* and *managing agents* must separately establish that *function*.

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

11 Group supervision

11.1 Application

11.1.1 R ...

11.1.1A R *SOLPRU* 11.1.2R to *SOLPRU* 11.11 (Mixed-activity holding companies) applies to the *Society* in circumstances where the *Society* is a member of an *insurance group*.

...

The following is new text and is not underlined.

13 Application of SOLPRU to Lloyd’s

13.1 Application

13.1.1 R *SOLPRU* 13 applies to the *Society* and, where specified, *managing agents*.

13.2 General application of SOLPRU to Lloyd’s: the Society and managing agents

- 13.2.1 R Where a provision in *SOLPRU* is expressed to apply to the *Society* “in accordance with” this rule, the *Society* must:
- (1) manage each *member’s funds at Lloyd’s*;
 - (2) carry out any applicable calculations in respect of each *member’s funds at Lloyd’s*;
 - (3) manage its *central assets* and *central liabilities*;
 - (4) where the context requires, supervise the *insurance business* carried on by each *member* at Lloyd’s; and
 - (5) take such further steps as may be required,
- in order to achieve, in relation to those assets and liabilities and that *insurance business*, the same effect as the relevant *SOLPRU* provision would have (that is, conforming with the requirements of any *rule* and taking appropriate account of any applicable *guidance*) when applied to a *firm* or to the *insurance business* of a *firm*.

- 13.2.2 R Where a provision in *SOLPRU* is expressed to apply to a *managing agent* “in accordance with” this rule, the *managing agent* must, in relation to each *syndicate* managed by it and for each *syndicate* year, manage:
- (1) the *syndicate assets* and liabilities; and
 - (2) the *insurance business* carried on by the *members* of the *syndicate* through that *syndicate*,
- in order to achieve, in relation to those assets and liabilities and that *insurance business*, the same effect as the relevant *SOLPRU* provision would have (that is, conforming with the requirements of any *rule* and taking appropriate account of any applicable *guidance*) when applied to a *firm* or to the *insurance business* of a *firm*.

13.3 Special provisions for Lloyd’s

- 13.3.1 R Neither the *Society* nor *managing agents* may permit a *member* to carry on any *insurance business*, except as a participant on one or more *syndicates*.
- 13.3.2 R The *Society* must ensure that all participants in the Lloyd’s market are made aware of their obligations under *SOLPRU*.
- 13.3.3 R The *Society* must establish and maintain effective arrangements to monitor and manage risk arising from:
- (1) conflicts of interest (including in relation to (2) to (4));

- (2) inter-*syndicate* transactions, including *reinsurance to close* and *approved reinsurance to close*;
- (3) related party transactions;
- (4) transactions between *members* and itself.

13.4 Approved reinsurance to close

- 13.4.1 G As defined in the *Glossary*, “approved reinsurance to close” excludes balance transfers between *syndicate years* of *syndicates* having only one *member*, which have no effect on the overall liabilities of that *member*.
- 13.4.2 G The “approved” status of an *approved reinsurance to close* does not alter the legal status or effect of the original *contract of insurance*, or the liability of a reinsured *member* to the *policyholder* under or in respect of the original *contract of insurance*.
- 13.4.3 R Notwithstanding that the liability of a reinsured *member* to a *policyholder* is unaffected by an *approved reinsurance to close* as described in *SOLPRU* 13.4.2G, for the purposes of *SOLPRU*:
- (1) for an *approved reinsurance to close* which is not to a *subsidiary* of the *Society*:
 - (a) a *contract of insurance* reinsured under an *approved reinsurance to close* must be treated as if the reinsuring *member* and not the reinsured *member* had effected the original *contract of insurance*; and
 - (b) any payment received by a *member* as consideration for or in connection with an *approved reinsurance to close* must be treated as a Lloyd’s *member’s contribution* and not as *premium* or as a *reinsurance recovery*;
 - (2) for an *approved reinsurance to close* to a *subsidiary* of the *Society*, a *contract of insurance* reinsured under that *approved reinsurance to close* must be treated as if the reinsured *member* had not effected the original *contract of insurance* but:
 - (a) for the purposes of the calculation of the Lloyd’s *SCR*, *general insurance business* carried on by *members* and *former underwriting members* which has been reinsured to a *subsidiary* of the *Society* under an *approved reinsurance to close* must be treated as reinsured to a third party; and
 - (b) for the purposes of calculating the *SCR* of any *subsidiary* of the *Society* which is a *UK Solvency II firm*, the approved reinsurance to close must be treated as a *reinsurance*.

13.5 Provision of information by managing agents

- 13.5.1 R A *managing agent* must, as soon as possible, give the *Society* any information the *managing agent* has concerning material risks to *funds at Lloyd's* or *central assets*.
- 13.5.2 R A *managing agent* need not comply with SOLPRU 13.5.1R if the *managing agent* knows that the *Society* already has the relevant information.

13.6 Insurance receivables to be carried to trust funds

- 13.6.1 R The *Society* must take all reasonable steps to ensure that each *member*:
- (1) executes the appropriate *Lloyd's trust deeds*; and
 - (2) carries to the appropriate *Lloyd's trust fund* all amounts received or receivable by the *member*, or on its behalf, in respect of any *insurance business* carried on by it.
- 13.6.2 R The *Society* must carry all amounts it receives on behalf of any *member* in respect of that *member's insurance business* to the appropriate *Lloyd's trust fund*.
- 13.6.3 R A *managing agent* must carry all amounts it receives on behalf of any *member* in respect of that *member's insurance business* to the appropriate *Lloyd's trust fund*.
- 13.6.4 R In complying with SOLPRU 13.6.1R to SOLPRU 13.6.3R, the *Society* and *managing agents* must take all reasonable steps to ensure that amounts received or receivable by a *member* in respect of *general insurance business* and *long-term insurance business* are carried to separate *Lloyd's trust funds*.

13.7 Amendments to byelaws, trust deeds and standard form letters of credit and guarantees

- 13.7.1 R The *Society* must, as soon as it is practical to do so, notify the *FSA* of its intention to approve the form of any new *Lloyd's trust deed*.
- 13.7.2 R The *Society* must, as soon as it is practical to do so, notify the *FSA* of its intention to make any amendment which may alter the meaning or effect of any *byelaw*, including:
- (1) any *Lloyd's trust deed*;
 - (2) any standard form letter of credit prescribed by the *Society* from time

- to time; or
- (3) any standard form guarantee agreement prescribed by the *Society* from time to time.
- 13.7.3 R The *Society* must provide the *FSA* with full details of:
- (1) the form of any new *Lloyd's trust deed* it intends to approve, as described in *SOLPRU* 13.7.1R; and
- (2) any amendments falling within *SOLPRU* 13.7.2R.
- 13.7.4 R The *Society* must consult interested parties in relation to any new *Lloyd's trust deed* and in relation to any amendment falling within *SOLPRU* 13.7.2R.
- 13.7.5 G Except in urgent cases, the *Society* should consult in relation to any new *Lloyd's trust deed* or amendments to any existing deed before the new deed or amendment take effect.
- 13.7.6 R The information provided to the *FSA* by the *Society* under *SOLPRU* 13.7.3R must include:
- (1) a statement of the purpose of any proposed amendment or new *Lloyd's trust deed* and the expected impact, if any, on *policyholders, managing agents, members, and potential members*; and
- (2) a description of the consultation undertaken under *SOLPRU* 13.7.4R including a summary of any significant responses to that consultation.
- 13.7.7 G The *FSA* would normally expect to receive the information required under *SOLPRU* 13.7.3R and *SOLPRU* 13.7.6R not less than three months in advance of the proposed change.

13.8 The Central Fund

- 13.8.1 R This section applies to the *Society*.
- 13.8.2 G The *rules and guidance* in this section are intended to promote confidence in the market at Lloyd's, and to protect certain *consumers* of services provided by the *Society* in carrying on, or in connection with or for the purposes of, its regulated activities. They do this by:
- (1) giving guidance to the *Society* about the protection that the *Central Fund* should provide for *policyholders*; and
- (2) enabling the *FSA* to keep under review the protection the *Central Fund* provides for *policyholders*.

Enabling provision

- 13.8.3 D The directions in this section are given under section 318 of the *Act* (Exercise of powers through Council) for the purpose of achieving the objective specified, as required by section 318(2) of the *Act*.
- 13.8.4 D The directions given in this section are given in relation to the exercise of the powers by the *Society* in respect of the *Central Fund* and are given with a view to achieving the objective of ensuring that the *Society* in making payments, or in providing any other financial assistance from the *Central Fund*, does so on a basis which does not take into account the amounts of compensation which *policyholders* may receive under the provisions of the *compensation scheme* in respect of *protected claims* against *members*.
- 13.8.5 G The *Society* should seek to ensure that the *Central Fund* provides protection for *policyholders* so as to minimise the need for Lloyd's *policyholders* to have recourse to the *compensation scheme*.
- 13.8.6 D The *Society* must, in the exercise of its powers to make payments from the *Central Fund* or to provide other forms of financial assistance from the *Central Fund*, ensure that in calculating and determining the amount of any such payment or the amount of any other financial assistance, it does not take into account the amounts of compensation which *policyholders* may receive under the provisions of the *compensation scheme* in respect of *protected claims* against *members*.

13.9 Capacity transfer market

- 13.9.1 R This section applies to the *Society*.
- 13.9.2 G The *rules* and *guidance* in this section are intended to promote confidence in the market at Lloyd's, and to protect certain *consumers* of services provided by the *Society* in carrying on, or in connection with or for the purposes of, its *regulated activities*. They do this by ensuring that the *Society* appropriately and effectively regulates the *capacity transfer market* so that it operates in a fair and transparent manner.
- 13.9.3 R The *Society* must make appropriate *byelaws* governing conduct in the *capacity transfer market*.
- 13.9.4 G The *byelaws* referred to in *SOLPRU* 13.9.3R should:
- (1) ensure that adequate and effective arrangements are in place to enable *members* and *persons* applying to be admitted as *members* to enter into transactions to transfer *syndicate* capacity and settle those transactions in a timely manner;
 - (2) give clear and comprehensive guidance about the dissemination of information that is, or may be, relevant to the price of *syndicate*

- capacity and the transparency of the *capacity transfer market*; and
- (3) prohibit unfair and abusive practices (including market manipulation), the misuse of information not generally available, and the dissemination of false or misleading information.
- 13.9.5 G The *Society* should have adequate and effective arrangements to:
- (1) record and monitor transactions in the *capacity transfer market*, and maintain adequate audit trails; and
- (2) suspend or annul transactions where appropriate.
- 13.9.6 G The *Society* should regularly review the *byelaws* referred to in *SOLPRU* 13.9.3R, taking into account the standards of conduct required in other *UK* financial markets.
- 13.9.7 G The *Society* should consult *members* and *underwriting agents* before it finalises material changes in the *byelaws* referred to in *SOLPRU* 13.9.3R, and should have timely and effective arrangements for notifying them of changes in those *byelaws*.

13.9 Former underwriting members

- 13.9.1 G The *rules* and *guidance* in this section are intended to promote confidence in the market at Lloyd's and to protect certain *consumers* of services provided by the *Society* in carrying on or in connection with or for the purposes of its *regulated activities*, by:
- (1) protecting policyholders against the risk that *former underwriting members* may not be able to meet any liabilities to carry out *contracts of insurance* that they underwrote at Lloyd's; and
- (2) enabling the *FSA* to impose requirements under section 320(3) of the *Act* (Former underwriting members) if it considers this appropriate to protect *policyholders*.
- 13.9.2 R The *Society* must ensure that sections 320 to 322 of the *Act* (Former underwriting members, Requirements imposed under section 320, Rules applicable to former underwriting members) are drawn to the attention of any *person* ceasing to be an *underwriting member* on or after *commencement*.
- 13.9.3 R The *Society* must require any person, other than a *body corporate*, ceasing to be an *underwriting member* on or after *commencement* to:
- (1) notify the *Society* of any change in his address within one month of the change; and
- (2) in the case of a natural person, to make arrangements for the *Society*

to be notified in the event of his death.

The following text is amended as follows. Underlining indicates new text and striking through indicates deleted text.

~~13~~ 14 Actions for damages

~~13.1~~ Application

14.1

~~13~~ 14.1.1 R A contravention of the *rules* in *SOLPRU* does not give rise to a right of action by a *private person* under section 150 of the *Act* (and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action).

...

Schedules

Sch 1 Record keeping requirement

...

Sch 2 Notification and reporting requirement

Sch 2.1 G The aim of the *guidance* in the following table is to give the reader a quick overall view of the relevant notification requirements.

...

Sch 2.3 G

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
	...			
<i>SOLPRU</i> 5.4.2R	Sufficient information to enable the <i>FSA</i> to understand the reasons why either of the limits referred to in <i>SOLPRU</i> 5.3.4R determines a <i>firm's MCR</i>	Sufficient information to enable the <i>FSA</i> to understand the reasons why either of the limits referred to in <i>SOLPRU</i> 5.3.4R determines a <i>firm's MCR</i>	Where either of the limits referred to in <i>SOLPRU</i> 5.3.4R determines a <i>firm's MCR</i>	Not specified

<u>SOLPRU 5.5.6R</u>	<u>If own funds attributable to an member fall below the reporting point determined in accordance with SOLPRU 5.5.5R</u>	<u>That own funds attributable to an member have fallen below the reporting point determined in accordance with SOLPRU 5.5.5R</u>	<u>Breach of the reporting point determined according to SOLPRU 5.5.4R</u>	<u>As soon as breach of reporting point observed by the Society</u>

<u>SOLPRU 12.5.1R</u>	Any major development affecting significantly the relevance of the information disclosed in the <i>firm's SFCR</i>	Information on the nature and effects of the major development. Where the major development concerns non-compliance with a <i>firm's MCR</i> or significant non-compliance with the <i>SCR</i> in the circumstances set out in <i>SOLPRU 12.5.3R</i> , the additional disclosure required by <i>SOLPRU 12.5.4R</i> to <i>SOLPRU 12.5.6R</i> , as applicable, must also be made	Any major development affecting significantly the relevance of the information disclosed in the <i>firm's SFCR</i> , including the matters set out in <i>SOLPRU 12.5.3R</i>	As specified in the <i>Solvency II Regulation</i> (except where immediate disclosure is required by <i>SOLPRU 12.5.3R</i> and as otherwise required by <i>SOLPRU 12.5.5R</i> and <i>SOLPRU 12.5.6R</i>)
<u>SOLPRU 13.7.1R</u>	<u>Society's intention to approve the form of any new Lloyd's trust deed</u>	<u>The form of any new Lloyd's trust deed, a statement of the purpose of the proposed amendment, expected impact on participants at Lloyd's, policyholders and potential members, and a description of the consultation undertaken required by SOLPRU 13.7.4R</u>	<u>Intention of Society to approve the form of any new Lloyd's trust deed</u>	<u>As soon as it is practicable to do so</u>
<u>SOLPRU</u>	<u>Any major</u>	<u>Full details of any</u>	<u>Society's</u>	<u>Not less than</u>

<u>13.7.2R</u>	<u>amendment which may alter the meaning or effect of any byelaw including the matters specified in SOLPRU 13.7.2R(1) to (3)</u>	<u>proposed amendment, a statement of the purpose of the proposed amendment, expected impact on participants at Lloyd's, policyholders and potential members, and a description of the consultation undertaken required by SOLPRU 13.7.4R</u>	<u>intention to make any amendment</u>	<u>three months in advance of the proposed change</u>
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Annex B**Amendments to the Glossary of Definitions**

In this Annex, underlining indicates new text. These new definitions should be inserted in the appropriate alphabetical position in the Glossary of definitions.

<i><u>central liabilities</u></i>	<u>the liabilities of the <i>Society</i>, excluding any liabilities of <i>members</i> (unless the <i>Society</i> has exercised its discretion to meet such liabilities) or any other participant at Lloyd's other than the <i>Society</i>.</u>
<i><u>central requirement</u></i>	<u>the calculation made by the <i>Society</i> pursuant to the requirements of <i>SOLPRU</i> 4.33 (Central requirement).</u>

Annex C

Amendments to the Supervision manual (SUP)

Note to reader: the amendments proposed in this Annex are based on the version of SUP 10 proposed in CP11/22 (Transposition of Solvency II), as well as the changes thereto proposed in Annex C of Appendix 1 of this consultation paper. In this Annex, underlining indicates new text and striking through indicates deleted text.

10 Approved persons

...

10.7.1A G A *UK Solvency II firm*, the *Society* and *managing agents* ~~are~~ is not required to appoint a *director* or *senior manager* to carry out the *apportionment and oversight function*. However, if:

- (1) a *UK Solvency II firm*, the *Society* or a *managing agent* chooses to appoint an *employee* to carry out some or all of the *apportionment and oversight function*; and
- (2) by carrying out the *apportionment and oversight function*, that *employee* will be effectively running the *firm* or will be responsible for some other key *function*;

the obligations on the *firm* to assess fitness and propriety in accordance with *SOLPRU* 9.8 (Fit and proper requirements) will apply and such *employee* is likely to be performing at least one other *controlled function* that is applicable to a *UK Solvency II firm*, the *Society* and *managing agents*.

...

Compliance oversight function

10.7.8 R The *compliance oversight function* is the function of:

- (1) for a *firm* that is not a *UK Solvency II firm*, the *Society* or a *managing agent*, acting in the capacity of a *director* or *senior manager* who is allocated the function set out in *SYSC* 3.2.8R or *SYSC* 6.1.4R(2);
- (2) for a *UK Solvency II firm*, the *Society* or a *managing agent*, acting in the capacity of an *employee* who is responsible for the compliance *function* set out in *SOLPRU* 9.4.1R(2).

...

Actuarial function (CF12) and *with-profits actuary function* (CF12A)

10.7.17 R The actuarial function is the function of:

- (1) for a *firm* that is not a *UK Solvency II firm*, the Society or a managing agent, acting in the capacity of an *actuary* appointed by a *firm* under *SUP* 4.3.1R to perform the duties set out in *SUP* 4.3.13R-;
- (2) for a *UK Solvency II firm*, the Society or a managing agent, acting in the capacity of an *employee* who is responsible for the actuarial *function* set out in *SOLPRU* 9.6.1R.

...

10.9 Significant management functions

Application

10.9.1 R *SUP* 10.9 applies only to a *firm* which:

- (1) under *SOLPRU* 9.2.3R(2)(a), *SYSC* 2.1.1R or *SYSC* 4.1.1R, apportions a significant responsibility, within the description of the *significant management function*, to a *senior manager* of a significant business unit; or
- (2) undertakes *proprietary trading*; or
- (3) (in the case of an *EEA firm*) undertakes the activity of *accepting deposits* from *banking customers* and activities connected with this; or
- (4) is a *UK Solvency II firm*, the Society, managing agent or *UK ISPV* that has individuals who are effectively running the *firm* or are responsible for other key *functions* that do not fall entirely within the scope of one or more of the other *controlled functions*.

...

Significant management function (CF29)

10.9.10 R

...

- (1A) ...
- (1B) In the case of a *UK Solvency II firm*, the Society, managing agent or *UK ISPV*, the *significant management function* also includes acting in the capacity of an individual who is effectively running the *firm* or has responsibility for a key *function*.

...

10.9.10 G For the purposes of *SUP* 10.9.10R(1B), it will be specific to the *person*, role and *firm* whether a *person* is effectively running a *UK Solvency II firm*, the Society, managing agent or *UK ISPV* or has responsibility for some other

key *function*. It may depend (for example) on how much influence or control a particular *person* has over the particular *firm*, or a key *function* within it. Therefore, each *firm* will need to form its own view about each relevant *person* and their role before deciding whether he is carrying out the *significant management function*. A *firm* should keep a careful record of each decision and the reasons for it. A *firm* should also review each decision if a material fact or circumstance changes.

...

10.12 Application for approval and withdrawing an application for approval

...

Who should make the application?

10.12.3 G ...

- (2) Usually this will be the *firm* that is employing the *candidate* to perform the *controlled function*. Where a *firm* has outsourced the performance of a *controlled function*, the details of the outsourcing determine where responsibility lies and whom the *FSA* anticipates will submit *approved persons* application forms. *SUP* 10.12.4G describes some common situations. The *firm* which is outsourcing is referred to as “A” and the person to whom the performance of the *controlled function* has been outsourced, or which makes the arrangement for the *controlled function* to be performed, is referred to as “B”. In each situation, A must take reasonable care to ensure that, in accordance with section 59(2) of the *Act*, no *person* performs a *controlled function* under an *arrangement* entered into by its contractor in relation to the carrying on by A of a *regulated activity*, without approval from the *FSA*. See also *SYSC* 3.2.4G and *SYSC* 8.1.1R; ~~and~~ for *insurers* other than *UK Solvency II firms*, the Society and managing agents see *SYSC* 13.9 and see *SOLPRU* 9.7 for *UK Solvency II firms*, the Society and managing agents.

Appendix 3

Public disclosure: Capital add-ons/Undertaking specific parameters

Annex

Amendments to the Prudential sourcebook for Solvency II Insurers (SOLPRU)

Note to reader: Amendments proposed in this annex are to the draft Handbook text as consulted on in CP11/22 (Transposition of Solvency II).

The following text is inserted after the chapter entitled “Action for damages” which is amended by Appendix 2 of this Consultation Paper to be SOLPRU 14. The text is a new section to the proposed SOLPRU sourcebook and is not underlined.

TP 1 Solvency and financial condition report: disclosure transitional

Application

1.1 R This section applies to:

- (1) a *UK Solvency II firm* that has been required by the *FSA* to:
 - (a) (as contemplated under *SOLPRU 4.11.2G*) replace a subset of the parameters used in the *standard formula* by *undertaking specific parameters* when calculating the life, non-life and health *underwriting risk* modules, where it is inappropriate to calculate the *SCR* in accordance with the *standard formula* because the *firm’s* risk profile deviates significantly from the assumptions underlying the *standard formula*; or
 - (b) (as contemplated under *SOLPRU 4.28.2G*) apply a *capital add-on* in circumstances where there has been a *standard formula significant risk profile deviation*, an *internal model significant risk profile deviation* or a *significant system of governance deviation*; and
- (2) a *UK Solvency II firm* that is a member of an *insurance group* that has been required by the *FSA* as the *group supervisor* to:
 - (a) replace a subset of the parameters used in the *standard formula* by parameters specific to the *insurance group* when calculating the life, non-life and health *underwriting risk* modules, where it is inappropriate to calculate the *group SCR* in accordance with the *standard formula* because the *insurance group’s* risk profile deviates significantly from the assumptions underlying the *standard formula*; or
 - (b) (as contemplated under *SOLPRU 11.5.10G*) apply a *capital add-on* in circumstances where there has been a *standard formula significant risk profile deviation*, an *internal model significant risk profile deviation* or a *significant system of governance deviation* at group level.

Purpose

- 1.2 G This section implements the third paragraph of article 51(2) of the *Solvency II Directive* which allows a discretion for the *capital add-on* and the impact of the *undertaking specific parameters* (or, as may be applicable, parameters specific to an *insurance group*) not to be separately disclosed during a transitional period.

Duration of transitional

- 1.3 R This section applies to a disclosure of the *SFCR* by a *firm* or, as may be applicable, the report on solvency and financial condition at the level of the *insurance group* by *participating Solvency II undertakings* or the *relevant insurance group undertakings* within the *insurance group*, made in relation to the relevant financial years ending on or before [31 December 2015].

Non-disclosure

- 1.4 R In the disclosure required by *SOLPRU 12.3.1R* (Public disclosure - solvency and financial condition report) or, *SOLPRU 12.3.1R* as applied to an *insurance group* by *SOLPRU 11.9.4R* (Group SFCR), a *firm* or an *insurance group* may, to the extent permitted by this section and unless required under other legal or regulatory requirements (including any *Solvency II EEA implementing measure*), opt not to disclose the following separately when disclosing the amount of the *MCR* and *SCR* (or, as may be applicable, *group SCR*) under *SOLPRU 12.3.5R*:
- (1) the information referred to in *SOLPRU 12.3.5R(2)* on any *capital add-on* imposed on the *firm* or, if the context so requires, the *insurance group*; and
 - (2) the information referred to in *SOLPRU 12.3.5R(3)* on any *undertaking specific parameters* or, if the context so requires, parameters specific to the *insurance group*.

Appendix 4

With-profits insurance business

Annex A

Amendments to the Prudential sourcebook for Solvency II Insurers (SOLPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text as against the proposed text of SOLPRU set out in CP 11/22 (Transposition of Solvency II Part 1)

2.4.7 R When calculating *technical provisions*, *firms* must take into account:

- (1) all expenses that will be incurred in servicing insurance and reinsurance obligations;
- (2) inflation, including expenses and *claims* inflation; and
- (3) all payments to *policyholders*, including future discretionary bonuses, which *firms* expect to make, whether or not those payments are contractually guaranteed,

but a firm carrying on *with-profits business* may exclude any *approved surplus funds*.

[2.4.8 G ~~For the purposes of SOLPRU 2.4.7R(3), a firm may exclude *approved surplus funds* if it obtains a waiver of SOLPRU 2.4.7R(3) under section 148 of the Act.~~]

Approved surplus funds

2.4.8 R For the purposes of SOLPRU 2.4.7R, a firm carrying on *with-profits business* must, in relation to a *with-profits fund*, determine the amounts that have not been made available for distribution to *policyholders*, for the purpose of calculating *approved surplus funds*, which must be no greater than the value of the assets in the *with-profits fund*, other than assets held to meet liabilities arising in connection with *non-profits insurance business*, less:

- (1) the value of asset shares attributable to *with-profits policies* in each *with-profits fund*, calculated in accordance with SOLPRU 2.4.18R and SOLPRU 2.4.19G, unless SOLPRU 2.4.20R applies in which case it is the item calculated in accordance with that rule; and
- (2) the adjustments to (1) set out, and calculated in accordance with, SOLPRU 2.4.23R,

in both cases determined in a manner consistent with the requirements on valuation in SOLPRU 2 and the *Solvency II Regulation*.

[Note: articles 78(3) and 91(2) of the *Solvency II Directive*]

Asset share calculation

...

2.4.17 G ...

2.4.18 R For the purpose of SOLPRU 2.4.8R(1), a firm must calculate asset share on the basis of the aggregate of asset share in respect of each *with-profits policy* or, if the result is likely to be the same or higher, the aggregate of the total asset share in respect of each group of *with-profits policies*, and in either case must take into account at least the following:

- (1) premiums received from the *policyholder*;
- (2) any expenses incurred or charges made (including *commissions*);
- (3) any partial benefits paid or due;
- (4) any investment income on, and any increases (or decreases) in, asset values;
- (5) any tax paid or payable and which is properly attributable in accordance with regulatory requirements to treat *customers* fairly;
- (6) any amounts received (or paid) under contracts of *reinsurance* or similar arrangements, where relevant to asset share;
- (7) any shareholder transfers and any associated tax paid or payable and properly attributable in accordance with regulatory requirements to treat *customers* fairly;
- (8) (a) enhancements representing any distributions which have been allocated to *policies*; or
 (b) enhancements and past miscellaneous surplus (or losses) which have been credited to (or debited from) asset share,
in each case where the intention is that the enhancements will be permanently included in payouts, even if the *firm* retains the right to reduce the enhancements in extreme circumstances;
- (9) the *firm*'s regulatory duty to treat its *customers* fairly and the need to ensure consistency with its *PPFM*.

2.4.19 G (1) In taking into account amounts in SOLPRU 2.4.18R(6) in order for the *firm* properly to identify amounts which are made available for distribution to *policyholders*, due regard should be had to the specific details of each relevant contract of *reinsurance* or similar arrangement and the relationship between the amounts received (or paid) and the value of the benefit granted (or received) under the arrangement. This should take into consideration, for example, the risk of default and differences in

the firm's assessment of the risks transferred and the contractual terms for such transfer of risk. Similar arrangements include securitisations and any other arrangements in respect of contracts of insurance that are similar to contracts of reinsurance in terms of the risks transferred.

- (2) Where allowance is made for shareholder transfers, this should be in respect of the accrued bonus entitlement reflected in the asset share. This would include both already declared discretionary additions to benefits under a with-profits policy made annually by the insurer and also accrued discretionary payments, in addition to the guaranteed benefits, which might be made when the benefits under the with-profits policy becomes payable. However, shareholder transfers in respect of amounts yet to be credited to asset share should not be charged to asset share until the corresponding amount is credited. A firm is required to make adequate provision for future shareholder transfers within the adjustments to be made in SOLPRU 2.4.23R.

Alternative calculation where asset share calculation inappropriate

2.4.20

R For the purposes of SOLPRU 2.4.8R(1), a firm:

- (1) may carry out an alternative calculation to the asset share calculation set out in SOLPRU 2.4.8R(1) to determine the amount made available for distribution to policyholders but only if the asset share calculation is inappropriate having regard to a particular with-profits policy or group of with-profits policies in question; and
- (2) must ensure that any alternative calculation is made taking into account at least the following items in relation to the particular with-profits policy or group of with-profits policies concerned in each with-profits fund, in order to determine the amount made available for distribution to policyholders:
- (a) future premiums;
 - (b) expenses to be incurred or charges to be made including commissions;
 - (c) benefits payable, including those set out in (3);
 - (d) any amounts to be received (or paid) under contracts of reinsurance or similar arrangement where relevant to with-profits policies being valued;
 - (e) tax payable
 - (f) shareholder transfers, if any, in respect of amounts

described in (3)(c), below.

and must ensure that adjustments are made as set out in SOLPRU 2.4.23R.

- (3) For the purposes of (2)(c) the benefits payable include:
- (a) all guaranteed benefits, including guaranteed amounts payable on death and maturity, guaranteed *surrender values* and paid-up values;
 - (b) vested declared and allotted bonuses to which *policyholders* are entitled; and
 - (c)
 - (i) future discretionary additions to benefits under a *with-profits policy* made annually by the *insurer*; and
 - (ii) discretionary payments, in addition to the guaranteed benefits, which might be made when the benefits under the *with-profits policy* becomes payable,

in each case at least equal to the levels required for the *firm* to fulfil its regulatory duty to treat its *customers* fairly; and
 - (iii) any allocation to *policies* of amounts based on the investment or other experience in the fund or more generally which has the effect or intention of permanently enhancing the measure for determining *policy* payments.

2.4.21 R A *firm* must take into account the *firm's PPFM* and its regulatory duty to treat its *customers* fairly when determining the items listed in SOLPRU 2.4.20R(2).

2.4.22 G The alternative method in SOLPRU 2.4.20R sets the calculation as the net present value of future cash flows listed in SOLPRU 2.4.20R(2).

Adjustments to the calculations referred to in SOLPRU 2.4.8R(1)

2.4.23 R For the purposes of SOLPRU 2.4.8R(2) a *firm* must make adjustments to the item calculated in accordance with SOLPRU 2.4.18R or 2.4.20R by including the sum of the amounts, as they relate to a particular *with-profits fund*, representing the value of assets less liabilities in respect of items (1) to (11), below, provided that no adjustments shall be made in relation to any amount that has already been included in the item calculated in accordance with SOLPRU 2.4.18R or SOLPRU 2.4.20R:

- (1) past miscellaneous surplus (or deficit) planned to be attributed to asset share but which has not yet been permanently credited to (or debited from) the item calculated in accordance with SOLPRU 2.4.18R or SOLPRU 2.4.20R;
- (2) planned deductions for the costs of guarantees, options and smoothing from the item calculated in accordance with SOLPRU 2.4.18R or SOLPRU 2.4.20R;
- (3) planned deductions for other costs deemed chargeable to the item calculated in accordance with SOLPRU 2.4.18R or SOLPRU 2.4.20R (other than those valued in (2));
- (4) future costs of contractual guarantees (other than financial options);
- (5) future costs in addition to those in (4) where the *firm* expects to pay further amounts to meet non-contractual commitments to *customers* or pay other benefits that need to be provided to fulfil the *firm's* regulatory duty to treat its *customers* fairly;
- (6) future costs of financial options, including guaranteed annuity and cash options;
- (7) future costs of smoothing carried out in accordance with generally accepted actuarial practice where the costs of smoothing may be negative;
- (8) future liabilities to repay financing costs of a *with-profits fund* where the *firm* expects to have to meet such liabilities and to the extent that these liabilities are not already provided for by amounts included in (11), below;
- (9) any other relevant liabilities, including further liabilities required for the *firm* to fulfil its regulatory duty to treat its *customers* fairly;
- (10) other *long-term insurance liabilities* to the extent that adequate provision has not been made in any other part of the adjustments set out in this *rule* for a particular fund; and
- (11) current liabilities, including accounting liabilities (including *long-term insurance liabilities* which have fallen due before the end of the *financial year*), liabilities from deposit back *reinsurance* arrangements where an amount is deposited with the *reinsurer* by the cedant, any provision for adverse variation, and any tax and other costs arising in respect of the recognition of future *shareholder transfers* or in respect of assets exceeding *insurance liabilities*.

2.4.24 G (1) SOLPRU 2.4.7R allows a *firm* carrying on *with-profits business* to

exclude approved surplus funds from its technical provisions. Approved surplus funds are considered by the PRA not to amount to insurance liabilities for the purpose of technical provisions. SOLPRU 2.4.7R is, therefore, the national law provision, referred to in article 91 of the Solvency II Directive, authorising certain surplus funds to be considered as not amounting to insurance liabilities. SOLPRU 2.4.8R sets out the way in which approved surplus funds must be calculated.

- (2) The effect of SOLPRU 2.4.18R to SOLPRU 2.4.23R is that a firm is not required to include the following items as liabilities relating to the payments it expects to make to policyholders:
- (a) any part of the with-profits fund surplus which has not already been allocated to policies for the purposes of determining the amount to be paid out when a claim is made;
 - (b) any planned enhancements in relation to a particular with-profits fund, not including enhancements described in SOLPRU 2.4.18R(8) or, if relevant, SOLPRU 2.4.20R(3)(c)(iii) and:
 - (i) which are not accounted for in any of the items calculated in accordance with SOLPRU 2.4.18R or SOLPRU 2.4.20R; and
 - (ii) where the firm retains discretion, legitimately and in accordance with regulatory requirements to treat its customers fairly, not to make such payments, in full or in part, in adverse circumstances leading to a deterioration in the financial position of the fund in question, for example as a result of adverse market movements.

[Note: articles 78(3) and 91(2) of the Solvency II Directive]

...

3 Own funds

...

3.2 Determination of own funds

...

Surplus funds

- 3.2.12 G Approved surplus funds will normally be classified as *Tier 1 own funds* (see *SOLPRU 3.3.7G*). For a firm operating a *with-profits fund*, *SOLPRU 2.4.8R* describes the maximum amount that a firm may claim as *approved surplus funds* for the purposes of excluding it from the calculation of *technical provisions*. Any such amounts must also satisfy the conditions for classification as *Tier 1 own funds* under *SOLPRU 3.3.2R*, including the characteristics in *SOLPRU 3.3.8R(1)*, namely that the item is ‘available’ to fully absorb losses on a going concern basis (as well as in the case of winding up). *Approved surplus funds* within a *with-profits fund* may satisfy *SOLPRU 3.3.8(1)* but still be subject to all of the restrictions imposed by virtue of their being in the *with-profits fund*, in particular, the ongoing considerations of fairness in relation to their use under regulatory requirements aimed at treating *with-profits policyholders* fairly.

Annex B

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Note to reader: One of the italicised terms is a new Glossary definitions related to, or used in, the proposed version of the Prudential sourcebook for Solvency II Insurers (SOLPRU) in CP11/22 (Transposition of Solvency II) which has not been made. The Glossary term marked with “*” is that which CP11/22 has proposed to amend; however, the amendment shown below supersedes that proposed amendment.

Insert the following new definition in the appropriate alphabetical position. The text is not underlined.

with-profits fund surplus The difference between:

- (1) the value of the assets of the *with-profits fund* identified in accordance with *COBS 20*; and
- (2) the value of the *technical provisions* in respect of the *policies* written out of or transferred into that *with-profits fund* and the value of the other liabilities, including those referred to in *COBS 20.1AR(1)*, in the fund;

calculated in accordance with *SOLPRU 2* and the *Solvency II Regulation*, and as determined by *actuarial investigation*.

Amend the following as shown.

actuarial investigation (other than in *COBS*) for a *firm* which is not a *UK Solvency II firm*, an investigation to which *IPRU-INS* rule 9.4 applies.

(in *COBS*) for a *UK Solvency II firm*, an investigation having regard to generally accepted actuarial practice, carried out once in every twelve-month period with advice, as appropriate, from the *persons* holding the *with-profits actuarial function* and the *actuarial function*.

*approved surplus funds** accumulated profits of a *UK Solvency II firm* which:

- (a) have not been made available for distribution to *policyholders*, determined in accordance with *SOLPRU 2.4.8R* and *SOLPRU 2.4.18R* to *SOLPRU 2.4.24G*; and
- (b) satisfy the conditions for classification as *Tier 1 own funds* under *SOLPRU 3.3.2R*.

- excess surplus* a firm will have an excess surplus in a *with-profits fund* if, and to the extent that:
- (a)
 - (i) if it is not a UK Solvency II firm, the regulatory surplus (or in the case of a realistic life firm the excess of realistic value of assets over realistic value of liabilities) in that with-profits fund; or
 - (ii) if it is a UK Solvency II firm, the with-profits fund surplus in that with-profits fund; and
 - (b) any other financial resources applied to, or expected to be applied to, that *with-profits fund*;
- exceed
- (c)
 - (i) if it is not a UK Solvency II firm, the amount required to meet the higher of any regulatory capital requirement or the firm's individual capital assessment (at the firm's own risk appetite) for existing business; or
 - (ii) if it is a UK Solvency II firm, the amount required to meet the higher of the notional SCR in relation to that with-profits fund and any capital provision determined in relation to the with-profits fund at the firm's own risk appetite as reflected in the firm's ORSA; and
 - (d) any further amount necessary to support the new business plans of that *with-profits fund*.
- inherited estate* for a firm other than a UK Solvency II firm, in relation to each with-profits fund, an amount representing the fair market value of the with-profits assets less the realistic value of liabilities, or, if not a realistic basis life firm, the regulatory value of liabilities, of a with-profits fund with-profits fund.
- for a UK Solvency II firm, in relation to each with-profits fund, an amount representing the value of the with-profits assets less the value of the technical provisions and other liabilities of the with-profits fund calculated in accordance with SOLPRU 2 and the Solvency II Regulation.
- with-profits assets* ~~assets that match~~ required to be included in the with-profits fund and which:
- (1) for a UK Solvency II firm, either meet technical provisions and other liabilities in respect of with-profits insurance business or represent a with-profits surplus which represent an excess of assets in the with-profits fund over the technical provisions in respect of insurance business written out of the fund and any other liabilities in the fund; or

- (2) for a firm that is not a UK Solvency II firm, either meet liabilities in respect of with-profits insurance business, or which represent an excess of assets in the with-profits fund over the technical provisions in respect of insurance business written out of the fund and any other liabilities in the fund.
- with-profits fund* (1) for a firm that is not a UK Solvency II firm (except in INSPRU):
- (a) a long-term insurance fund (or that part of such a fund) in which policyholders are eligible to participate in any established surplus); and
- (b) where it is an insurer's usual practice to restrict participation in any established surplus to that arising from only part of the fund (or part fund) falling within (a), that part (or that part of the part fund).
- (2) for a UK Solvency II firm:
- subject to (c), is comprised of the items set out in (a) adjusted to take account of the outgoings in (b):
- (a) (i) premiums and other receivables in respect of with-profits policies;
- (ii) other receipts of the business of effecting or carrying out with-profits policies including but not limited to tax receipts;
- (iii) assets identified as available to cover its insurance liabilities arising from the business of effecting or carrying out with-profits policies including:
- (A) as required in COBS 20.1A.4R;
- (B) as identified in the policy documentation, PPFM, or other communications by the firm with policyholders or by virtue of the firm's established practice, as being available for that purpose; and
- (C) any other assets identified by the firm as being available for that purpose;
- but excluding:
- (D) assets which the firm has stated to be available only on the occurrence of a contingent event and which have not

been identified by the firm as restricted to covering the liabilities referred to in (iii);

- (iv) all income and capital receipts in respect of the items in (a)(i) to (iii);
- (v) assets into which the items in (i) to (iv) have been converted, including assets representing investment in *non-profit insurance business*; and
- (vi) premiums, receivables, other receipts, income and capital receipts from, and assets identified by the firm as available to cover its insurance liabilities arising out of, *non-profits insurance business* falling within (v) or otherwise written with the support of assets in (i) to (iv);

(b) outgoings:

- (i) outgoings in respect of the firm's business of effecting or carrying out *with-profits policies* and, if relevant, *non profits insurance contracts* written using the support of or as an investment of assets in (a) above;
- (ii) transfers made in accordance with COBS 20.1A.8R;

(c) where COBS 20.1A.2R applies, each sub-fund identified in accordance with that provision shall constitute a separate *with-profits fund*.

- (3) For the purposes of *INSPRU*, a *long-term insurance fund* in which *policyholders* are eligible to participate in any *established surplus*.

with-profits insurance business the business of *effecting* or carrying out ~~*with-profits insurance contracts*~~. *with-profits policies*.

with-profits policy ~~a contract falling within the class of *long-term insurance business* which is eligible to participate in any part of any *established surplus*.~~

a *long-term insurance contract* which provides benefits through, at least in part, eligibility to participate materially in periodic discretionary distributions based on profits arising from the firm's business or from a particular part.

Annex C

Amendments to the Prudential Sourcebook for Insurers (INSPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.5 Internal-contagion risk

...

- 1.5.30 R (1) A *firm* must apply or use a *long-term insurance asset* only for the purposes of its *long-term insurance business*.
- (2) For the purposes of (1), applying or using an asset includes coming under any obligation (even if only contingently) to apply or use that asset.
- 1.5.31 R A *firm* must not agree to, or allow, any mortgage or charge on its *long-term insurance assets* other than in respect of, and for the purposes of, a *long-term insurance liability*.

Annex D

Amendments to the Supervision manual (SUP)

In this Annex, underlining indicates new text and striking through indicates deleted text.

4.3 Appointment of actuaries

...

4.3.16A R ...

- (6) advise the *firm* as to the data and systems that he reasonably considers necessary to be kept and maintained to provide the duties in (5); ~~and~~
- (7) in the case of a *friendly society* to which this section applies, perform the function of appropriate actuary under section 12 (Reinsurance) of the Friendly Societies Act 1992 or section 23A (Reinsurance) of the Friendly Societies Act 1974 as applicable, in respect of those classes of its *with-profits business* covered by his appointment; ~~and~~
- (8) advise on any actuarial investigation required to determine the with-profits-fund surplus.

Annex E

Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Part 1: Comes into force on 1 January 2014

20.1 Application

...

20.1.3 R For an *EEA insurer*:

(1) (a) the rules and guidance on the with-profits fund (COBS 20.1A) apply only in so far as responsibility for the matter in question has not been reserved to the firm's Home State regulator by an EU instrument;

(b) the rules and guidance on treating with-profits policyholders fairly (COBS 20.2.1G to COBS 20.2.41G and COBS 20.2.53R to COBS 20.2.60G) and the governance provisions in COBS 20.5 apply only in so far as responsibility for the matter in question has not been reserved to the firm's Home State regulator by a European Community an EU instrument;

notwithstanding the above:

(c) COBS 20.2.26AR (financial penalties and the with-profits fund) applies;

(d) the rules and guidance on the notification of policyholders where there is a change in the percentage allocation of distributions (COBS 20.2.19AR to 20.2.19CG) apply but only to the extent that the United Kingdom is the state of the commitment;

...

(3) the rule on providing information to with-profits policyholders who are habitually resident in where the United Kingdom is the state of the commitment (COBS 20.4.4R) and the rule on production and provision of a CFPPFM (COBS 20.4.5R) apply, but the rest of COBS 20.4 (Communications with with-profits policyholders) does not; and

(4) the rule on production and provision of a CPPFM (COBS 20.4.5R) applies as if a reference to a firm was a reference to an

EEA insurer in relation to any of its *with-profits policyholders* ~~who are habitually resident in~~ where the state of the commitment is the United Kingdom; and

- (5) references to a *with-profits fund* in COBS 20 apply as if they were references to the relevant fund established in accordance with the requirements of the *home state*.

The following section (COBS 20.1A) is all new and is not underlined. Insert new section after COBS 20.1 as follows.

20.1A The with-profits fund

‘Other liabilities’ in the with-profits fund

20.1A.1 R For the purposes of calculating any *with-profits funds surplus*, *with-profits assets* and *inherited estate*, and the *rules* and *guidance* in relation to the governance and management of the *with-profits fund*, including COBS 20.1A.5R and COBS 20.1A.6R, a *firm* must include the following as ‘other liabilities’:

- (1) planned enhancements referred to in SOLPRU 2.4.24G(2)(b); and
- (2) unless expressly excluded in the context of a particular provision, the value of prospective future transfers out of the *with-profits fund* attributable to shareholders in accordance with the *rules* and *guidance* in COBS 20, calculated in accordance with SOLPRU 2 and the *Solvency II Regulation*, save to the extent that this item has been appropriately taken into account in the calculation of *technical provisions*.

Sub funds

20.1A.2 R (1) Where the *firm*:

- (a) identifies particular assets in connection with a particular part of its *with-profits fund*; and
- (b) restricts discretionary additions to *policy* benefits to those arising from the investment or other experience of only that part of the fund,

then, provided that:

- (c) such identification and restriction is consistent with the considerations in (3), and
- (d) treats each affected category of *with-profits policyholder*

fairly, having regard to those considerations,

each such part constitutes a separate *with-profits fund*.

- (2) Notwithstanding (1), each different part of its *with-profits fund* constitutes a separate sub-fund if that is necessary in order to treat each affected category of *with-profits policyholder* fairly, having regard to the considerations in (3).
- (3) The considerations referred to in (1) and (2) are the terms of the relevant *with-profits policies*; the *firm's* established practice; its *PPFM* and/or other relevant communications to affected *with-profits policyholders*.

20.1A.3 G For the purposes of *COBS* 20.1A.2R, the following may be relevant considerations when a *firm* determines whether its arrangements give rise to sub-funds amounting to separate *with-profits funds*.

- (1) If a *firm* places any restrictions on applying assets such that those assets, and/or any value of those assets in excess of *technical provisions* and other liabilities, can only be used for particular *policyholders*, *policies* or to meet losses arising from particular risks, then, subject to (4) and (5) below, that may tend to indicate that the assets and associated liabilities constitute a separate *with-profits fund*.
- (2) The fact that two (or more) different groups of *policyholders* may have different types of interests in a single pool of assets does not, of itself, give rise to separate sub-funds. For example, two different bonus series within a *with-profits fund* or different minimum guarantee bonus levels would not, of itself, give rise to separate sub-funds.
- (3) If two pools of assets are managed in different ways this does not, of necessity, mean that they are different *with-profits funds*. For example, a different mixture of assets might be used for life and pensions business, for contracts with and contracts without onerous guarantees, for contracts close to and those further from maturity, or for the *inherited estate* compared with the rest of the *with-profits fund*. Likewise, if a *firm* provisionally allocates assets for different product groups that will not, of itself, create a separate sub-fund.
- (4) A *firm* should consider its particular arrangements to determine which *policyholders'* claims are covered (from a contractual or fairness basis) by the assets in the pools, taking into account what *policyholders* had been told they were entitled to, including by reference to the *PPFM* and other relevant communications. Where there is a conflict between what different *policyholders* have been told and the *firm's* arrangements, then the *firm* would be expected to demonstrate that any segregation into separate *with-*

profits funds, or non-segregation, would be fairly proportioned between the relevant groups of *policyholders* in the particular circumstances, taking into account the views of the *with-profits committee* or *with-profits alternative arrangement*.

- (5) Sub-funds may arise following a court process requiring separation of, or a restriction on, assets. For example, in a *retribution*, electing *policyholders* may no longer have a claim to the *inherited estate*, while non-electing *policyholders* do, depending on the terms of the scheme. Therefore, these two groups of *policyholders* would have claims to different pools of assets which the *FSA* considers may give rise to two separate *with-profits funds*.
- (6) Each *with-profits fund* will be treated as a separate *ring-fenced fund* for the purposes of *SOLPRU 3.2.11G*.

Governance arrangements for the with-profits fund

- 20.1A.4 R A *UK Solvency II firm* effecting or carrying out *with-profits insurance business* must identify the assets relating to all the business written into each *with-profits fund* which it is required to hold by virtue of *COBS 20.1A.5R*.
- 20.1A.5 R A *UK Solvency II firm* must ensure that it holds *assets* in each of its *with-profits funds* of a value sufficient to cover the *technical provisions* and other liabilities in respect of all of the business written into that *with-profits fund*.
- 20.1A.6 R A *UK Solvency II firm* must maintain separate accounting records in respect of each of its *with-profits funds*. The accounting records must identify:
- (1) all of the assets of that *with-profits fund*;
 - (2) the *technical provisions* in respect of the *with-profits policies* written into that *with-profits fund*;
 - (3) the *technical provisions* in respect of the *non-profit insurance contracts* written into that *with-profits fund*;
 - (4) any other liabilities of the *with-profits fund* not covered by (2) or (3), and their value calculated in accordance with *SOLPRU 2* and the *Solvency II Regulation*.
- 20.1A.7 G A *UK Solvency II firm* must ensure that the assets in its *with-profits funds* are separately identified and allocated to the relevant *with-profits fund* at all times. Assets in external accounts, for example at banks, custodians, or brokers should be segregated in the *firm's* books and records into separate accounts for *with-profits insurance business* and other business. Where a

firm has more than one *with-profits fund*, separate accounting records must be maintained for each fund. Accounting records should clearly document the allocation.

- 20.1A.8 R A *UK Solvency II firm* must not transfer assets out of a *with-profits fund* unless:
- (1) the assets represent any part of a *with-profits fund surplus*, or represent assets held in accordance with *COBS 20.1A.5R* in relation to the part of a distribution that has been made which is properly attributable to shareholders, in accordance with *COBS 20*; and
 - (2) no more than three months have passed since the *actuarial investigation* determining that surplus.
- 20.1A.9 G For the purposes of *COBS 20.1A.8R*, an *actuarial investigation* is required to determine any *with-profits fund surplus* for the purposes of the requirements in *COBS 20* and remains in-date for three months from the date as at which the determination of the surplus was made. However, even where the investigation is still in-date, the *firm* should not make the transfer unless there is sufficient surplus at the time of the transfer to cover the value of the assets being transferred. The *actuarial investigation* carried out may rely in part on any relevant and sufficiently up-to-date valuation exercise carried out for the purposes of calculating *technical provisions* under *SOLPRU* and the *Solvency II Regulation* provided that the person carrying out the *actuarial investigation* considers it appropriate to do so.
- 20.1A.10 R (1) A *UK Solvency II firm* must use or apply an asset in a *with-profits fund* only for the purpose of the business in the *with-profits fund*.
- (2) For the purpose of (1), applying or using an asset includes any obligation (even if only contingently) to apply or use that asset.
- 20.1A.11 R A *UK Solvency II firm* must not agree to, or allow, any mortgage or charge on the assets in any of its *with-profits funds*, other than in respect of, and for the purposes of, the business in the *with-profits fund*.
- 20.1A.12 G References in *COBS 20.1A.10R* and *COBS 20.1A.11R* to ‘the purposes of the business’ in the *with-profits fund* include the payment of claims, expenses and liabilities arising from that business, the acquisition of lawful access to fixed assets to be used in that business and the investment of assets. The payment of liabilities may include repaying a loan but only where that loan was incurred for the purpose of the business written into the *with-profits fund*. The purchase or investment of assets may include an exchange at fair market value of assets (including cash) between the *with-profits fund* and other assets of the *firm*. A *UK Solvency II firm* may also lend securities held in a *with-profits fund* under a stock lending transaction, or transfer assets as collateral for a stock lending transaction, where the *firm* is the borrower and where such lending or transfer is for

the benefit of the business written into the *with-profits fund*.

- 20.1A.13 G For the avoidance of doubt, assets derived from *premiums*, receivables, assets identified, or other receipts in respect of *with-profits policies* and any *non-profit insurance contracts* written into the *with-profits fund* (net of any policy outgoings properly payable from the fund), continue to comprise part of the *with-profits fund* whether or not the benefits under the *policies* to which those *premiums* receivable and assets originally related remain in force. This means that, in general, any *inherited estate* forms part of the *with-profits fund*.

Management of the with-profits fund

- 20.1A.14 R A *UK Solvency II firm* which is subject to contractual terms providing for payments under a *capital instrument* included in that *insurer's own funds*, must:
- (1) manage any *with-profits fund* so that discretionary benefits under a *with-profits policy* are calculated and paid, disregarding, insofar as is necessary for its *customers* to be treated fairly, any requirements in such contractual terms whether or not such requirements are absolute, contingent or at the discretion of the *firm*; and
 - (2) disclose its intention to manage the *with-profits fund* on the basis set out in (1) in the *firm's PPFM*.
- 20.1A.15 G (1) A *UK Solvency II firm* is expected to manage its *with-profits fund* so that amounts (whether interest, principal, or other outgoings) payable by the *firm* under a *capital instrument* included in that *insurer's own funds* do not impact on the *with-profits fund's* assets nor on the *firm's* ability to declare and pay under a *with-profits policy* discretionary benefits that are consistent with the *firm's* obligations under *Principle 6* (Customers' interests).
- (2) A *firm*, other than a *mutual*, should not regard any asset held in the *with-profits fund* as necessarily available to cover distributions or other obligations arising under a subordinated loan.
- 20.1A.16 R A *UK Solvency II firm* must ensure that it has adequate arrangements in place for ensuring that transactions affecting the assets of the *firm* operate fairly between *with-profits policyholders* and other persons interested in the other assets of the *insurer*, and where the *firm* has more than one *with-profits fund* those transactions operate fairly between the *with-profits policyholders* in each of those funds.

20.2 Treating with-profits policyholders fairly

...

- 20.2.5 R ...
- (3) A *firm* must calculate unsmoothed asset share by:
- (a) (i) for a *firm* which is not a *UK Solvency II firm*, applying the methods in *INSPRU* 1.3.119R to *INSPRU* 1.3.123R;
- (ii) for a *firm* which is a *UK Solvency II firm*, applying the methods in *SOLPRU* 2.4.18R to *SOLPRU* 2.4.20R;

...

...

Conditions relevant to distributions

- 20.2.16B G References to distributions in *COBS* 20 includes distributions of distributable profits arising, namely any permanent addition to *policy* benefits made at the *firm*'s discretion based on the investment or other experience in the fund or more generally. Distributions include those relating to expected payments for which allowance has or had already been made in the *technical provisions*, or those relating to other liabilities, such as planned enhancements referred to in *SOLPRU* 2.4.24G(2)(b), and not just distributions of any *with-profits fund surplus*.
- 20.2.16C G Examples of distributions include any payment of a cash bonus (including a final bonus on exit or a reduction in *premium*), or a declaration of a reversionary bonus in the form of a permanent addition to the benefits guaranteed to be payable at death or on maturity. In *COBS* 20.2.21R and *COBS* 20.2.22E (distributions from *excess surplus*) distributions also include any other amounts that are added to asset shares or to any other measure that is used to determine payouts under *policies*.
- 20.2.17 R A *firm* must:
- (1) not make a distribution from a *with-profits fund*, unless
- (a) if it is not a *UK Solvency II firm* the whole of the cost of that distribution can be met without eliminating the *regulatory surplus* in that *with-profits fund*; and
- (b) if it is a *UK Solvency II firm*:
- (i) the whole of the cost of that distribution can be met without eliminating the *with-profits fund surplus* in that *with-profits fund*; and
- (ii) following any distribution that relates to planned enhancements described in *SOLPRU*

2.4.24G(2)(b), the firm is able to demonstrate that it reasonably expects to be able to continue to comply with the requirements in COBS 20.1A.5R; and

(2) ...

...

20.2.18 R A firm which is not a UK Solvency II firm, and which is a realistic basis life firm must not make a distribution from a with-profits fund to any person who is not a with-profits policyholder, unless the whole of the cost of that distribution (including the cost of any obligations that will or may arise from the decision to make a distribution) can be met from the excess, if any, of the realistic value of assets over the realistic value of liabilities in that with-profits fund.

20.2.19 R ...

Notification and other requirements in relation to certain distributions

20.2.19A R If a firm which is a Solvency II undertaking proposes to make a distribution from a with-profits fund to any person who is not a with-profits policyholder, where:

(1) the distribution to policyholders is smaller than the ‘pre-notification to policyholder minimum’ calculated in accordance with COBS 20.2.19BR(1) then the firm must:

(a) provide the FCA with written details of the proposed distribution at least four months prior to the proposed distribution, together with copies of draft notifications it proposes to send to policyholders to satisfy (b); and

(b) give affected policyholders in the fund at least three months prior written notice stating:

(i) that it proposes to make no distribution to them, or

(ii) that it proposes to make a distribution of an amount which is smaller than the ‘pre-notification to policyholder minimum’, and setting out the amount and how the distribution is calculated; and

(iii) the reasons for (i) or (ii) as relevant; or

(2) the distribution to policyholders does not meet the test in (1) but is greater than the ‘after the event notification to policyholder minimum’ calculated in accordance with COBS 20.2.19BR(2) then the firm must:

- (a) provide the FCA with written details of the proposed distribution at least one month's prior to the proposed distribution together with copies of draft notifications it proposes to send to *policyholders* to satisfy (b); and
- (b) give affected *policyholders* in the fund notice of the distribution within a reasonable period from the date of the distribution, setting out the amount of the distribution, how it was calculated and the reasons for the change compared to the last previous distribution.

20.2.19B R (1) The 'pre-notification to *policyholder* minimum' referred to in *COBS 20.2.19AR* is as follows:

$$\frac{\mathbf{b \times c}}{\mathbf{a}} - \frac{\mathbf{c}}{50}$$

where

a is the total amount available for distribution to *policyholders* of the *with-profits fund* in question at the time of the most recent previous distribution to *policyholders*;

b is the amount of the most recent previous distribution to *policyholders*; and

c is the total amount available for distribution in relation to the proposed distribution.

(2) The 'after the event notification to *policyholder* minimum' referred to in *20.2.19AR* is as follows:

$$\frac{\mathbf{b \times c}}{\mathbf{a}} - \frac{\mathbf{c}}{200}$$

where **a**, **b** and **c** have the same meaning as in (1).

20.2.19C G (1) *COBS 20.2.19AR*(1) and *COBS 20.2.19BR* are aimed at ensuring that the *FCA* and relevant *policyholders* are appropriately pre-notified if the *firm* proposes a distribution to *policyholders* which is more than two per cent lower, in real terms, than the distribution last allocated to them.

(2) If the circumstances described in *COBS 20.2.19AR*(1) or (2) arise, then the *firm* should also consider whether any reduction(s) in the proposed distribution and any previous distributions to *policyholders* over a period of at least the previous five years are consistent with treating *policyholders* fairly and any other obligations of the *firm* under *COBS 20*.

- (3) When calculating the amounts distributed in COBS 20.2.19AR and COBS 20.2.19BR:
- (a) any amount allocated to *policyholders* in anticipation of a distribution is treated as included in the next distribution; and
- (b) the amount of any available distributable profits is treated as reduced by any part of it which the *firm* has decided to carry forward unappropriated.
- (4) A *firm* which is not a *Solvency II undertaking* is required to comply with *IPRU(INS) 3.3*.

...

20.2.25 R A proprietary *firm* may pay compensation or redress due to a *policyholder*, or former *policyholder*, from assets attributable to shareholders, whether or not they are held within a *long-term insurance fund* or *with-profits fund*, as relevant.

...

20.2.26 R ...

20.2.26A R A *firm* must not charge to a *with-profits fund* any financial penalty imposed on the *firm* by the *FSA*.

...

20.2.32 R Unless *COBS 20.2.32AR* applies, a *firm* carrying on *with-profits business* must not...

20.2.32A R *COBS 20.2.32R(1)* does not apply to a *UK Solvency II firm* carrying on *with-profits business*.

20.3.32B G Loans to a *connected person* using assets in a *with-profits fund* should be considered as investments of assets within the *with-profits fund*. As such, a *UK Solvency II firm* will need to ensure that such loans comply with *SOLPRU 7* having regard to *COBS 20.2.35AG* and, in the reasonable opinion of the *firm's* senior management, are in the best interests of the *with-profits policyholders* in the relevant *with-profits fund*.

20.2.33 G (1) If a *firm*, or a *connected person*, provides support to a *with-profits fund* (for example, by a contingent loan), by a transfer of assets into the fund, no reliance should be placed on that support when the *firm* assesses the *with-profits funds* financial position should not be considered to be available as an asset of the *with-profits fund* unless there are clear and unambiguous criteria governing any repayment obligations to the support provider.

- (2) For the purposes of managing the *with-profits fund*, the degree of reliance placed on that support asset should depend on the subordination of the support to the fair treatment of continuing availability of the asset for the benefit of *with-profits policyholders* and clarification of what fair treatment means in various circumstances. For a *firm* that is not a *UK Solvency II firm* and which is a *realistic basis life firm* this would normally be evidenced by the liability for such support being capable, under stress, of a progressively lower valuation in the *future policy-related liabilities*.

20.2.34 G Where assets from outside a *with-profits fund* are made available to support that fund (and there is no ambiguity in the criteria governing any repayment obligations to the support provider), a *firm* should manage the fund disregarding the liability to repay those assets, at least in so far as that is necessary for its policyholders to be treated fairly taking those assets into account solely to the extent the arrangements have been formally approved by a court or, in relation to a *friendly society*, the *FSA*.

- 20.2.34A R (1) A *UK Solvency II firm* must ensure that, in relation to any assets outside a *with-profits fund* providing support to it:
- (a) the precise terms and conditions on which those support assets operate and may become available, including whether and when they are repayable,
 - (i) are adequately documented in the *firm's* records; and
 - (ii) if the *firm* is required to produce a *PPFM*, are set out clearly and unambiguously in its *PPFM*, and an appropriate description is set out in the *CFPPFM*.
 - (b) the operation of those support assets is consistent with terms and conditions set out in communications to *with-profits policyholders* including any *PPFM* and *CFPPFM*.

Other rules and guidance on the conduct of with-profits business

20.2.35 G When a *firm*, other than a *UK Solvency II firm*, determines its investment strategy ...

20.2.35A G A *UK Solvency II firm* is required to consider its investment strategy in relation to the assets in a *with-profits fund*, including any *strategic investments* in accordance with *SOLPRU 7*. *Firms* are expected, in applying *SOLPRU 7*, to take into account the particular circumstances and requirements of the liabilities in the relevant *with-profits fund* to which those assets relate. For example, a *UK Solvency II firm* will need to consider whether a *strategic investment* meets the criteria set out in *SOLPRU 7.2*, that the investment will ensure the quality, security,

liquidity of the portfolio of assets of the *firm* as a whole and that the investment(s) are localised to ensure their availability. Where there is a conflict of interest (eg, between the *with-profits policyholders* and the *firm*) the *firm* must ensure that the *strategic investment* is made in the best interests of *policyholders*. It is expected that a *UK Solvency II firm* applying the provisions set out in *SOLPRU 7* in this manner will lead to *with-profits policyholders* being treated no less fairly than if the *firm* was not a *UK Solvency II firm* subject to *COBS 20.2.35G* and *COBS 20.2.36R*.

20.2.36 R A *firm*, other than a *UK Solvency II firm*, must not:

- (1) use *with-profits assets* to finance the purchase of a *strategic investment*, directly or by or through a *connected person*; or
- (2) retain an investment referred to in (1);

unless its *governing body* is satisfied, so far as it reasonably can be, and can demonstrate, that the purchase or retention is likely to have no adverse effect on the interests of its *with-profits policyholders* whose *policies* are written into the relevant fund.

...

20.2.36B G ...

- (2) A *firm* should also consider whether making or retaining ~~the investment~~ a *strategic investment* should be disclosed to *with-profits policyholders*.

...

20.3 Principles and Practices of Financial Management

...

20.3.5 R A *firm's PPFM* must cover...

- (1) ...; ~~and~~
- (2) ...; and
- (3) the precise terms and conditions of any other support assets as described in *COBS 20.2.34AR*.

20.4 Communications on with-profits policyholders

...

Requirements on EEA insurers

20.4.4 R In relation to any *with-profits policyholder* ~~who is habitually resident in where the member state of the commitment is the United Kingdom~~, an *EEA insurer* must:

- (1) ~~on request~~, provide the information necessary to enable that *policyholder* properly to understand the *insurer's* commitment under the *policy*;
- (2) ensure that the information provided is not narrower in scope or less detailed in content than the information required to be provided in the equivalent-PPFM produced by a firm subject to COBS 20.3; and
- (3) ...

...

20.5 With-profits governance

...

20.5.3 R A *firm* must ensure that the *terms of reference* contain, as a minimum, terms having the following effect:

...

- (2) that the *with-profits committee* or advisory arrangement must:

...

- (b) in any event give appropriate consideration to the following non-exhaustive list of specific matters:

...

(ix) ...; and

(x) ...;

(xi) the identification and extent of the firm's with-profits funds, with particular regard to the considerations in COBS 20.1A.2R and COBS 20.1A.3G; and

(xii) the use and purpose of, and terms under which, support assets are available to the with-profits fund, having regard to the considerations in COBS 20.2.34AR.

TP 2 Other Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provisions: coming into force
...					
<u>2.23</u>	<u>all rules and guidance in COBS 20 referring to the with- profits fund and in relation to TP 2.23R(2), COBS 20.1A.2R.</u>	<u>R</u>	<p><u>(1) For firms operating a with-profits fund prior to 1 Jan 2014:</u></p> <p><u>(a) assets in the with-profits fund on 31 December 2013 are deemed to comprise items in a with-profits fund for the purposes of COBS 20 from 1 January 2014, provided that any transfers out of, and any outgoings from, the fund up to 31 December 2013 were made in accordance with, and/or do not on 31 December 2013, constitute, or continue to constitute, a breach of, the rules and guidance in INSPRU 1.5.21R and 1.5.27R, but subject to (2) below;</u></p> <p><u>(b) any assets transferred out of the fund in breach of INSPRU 1.5.21R and 1.5.27R are deemed not to have been transferred out of the fund and remain part of the with-profits fund;</u></p> <p><u>(c) to the extent that the assets referred to in (b) have also been transferred out of the</u></p>	<u>1 January 2014 to 1 January 2015</u>	<u>1 November 2007</u>

			<u>firm then, before (a) can apply to the firm, the firm must transfer into the with-profits fund assets equal to the value of the assets referred to in (b), and of a similar quality, having regard to SOLPRU 7.</u>		
			<u>(2) Firms to which (1)(a) applies must, in any event, comply with COBS 20.1A.2R and (1)(a) does not apply if COBS 20.1A.2R requires a firm to create or make changes to sub-funds amounting to separate with-profits funds prior to 1 January 2014.</u>	<u>1 January 2014 to 1 January 2015</u>	<u>1 January 2014</u>

...

Sch 1: Record keeping requirements

...

Sch 1.3G

...				
COBS 19.2.3 R	...			
<u>COBS 20.2.34 AR(1)(a)(i)</u>	<u>Support assets outside the with-profits fund</u>	<u>Precise terms and conditions on which support assets operate and are available including whether and when they are repayable</u>	<u>when a firm first has support assets outside the with-profits fund</u>	<u>Until the firm ceases to use support assets outside the with-profits fund</u>
...				

Sch 2: Notification requirements**Sch 2.1G**

Handbook reference	Matters to be notified	<u>Contents of notification</u>	<u>Trigger event</u>	<u>Time allowed</u>
<u>COBS 2.2.19AR(1)</u>	<u>Details of a proposed distribution.</u>	<u>Written details of the proposed distribution, together with copies of draft notifications it proposes to send to policyholders.</u>	<u>The proposed distribution to policyholders is smaller than the 'pre-notification to policyholder minimum' calculated in accordance with COBS 20.2.19BR(1).</u>	<u>At least four months prior to the proposed distribution</u>
<u>COBS 2.2.19AR(2)</u>	<u>Details of a proposed distribution.</u>	<u>Written details of the proposed distribution, together with copies of draft notifications it proposes to send to policyholders.</u>	<u>The distribution to policyholders does not meet the test in COBS 20.2.19AR(1) but is greater than the 'after the event notification to policyholder minimum' calculated in accordance with COBS 20.2.19BR(2).</u>	<u>At least one month prior to the proposed distribution</u>
<u>COBS 20.2.45R</u>	...			
...				
<u>TP 2.9B</u>	<u>A firm falling within COBS TP 2.9B(1) must provide the appropriate regulator with sufficient notice of any application it makes to court for the purposes of COBS TP 2.9B(1) in order to allow</u>	<u>Details of any application it proposes to make to court for the purposes of COBS TP 2.9B(1).</u>	<u>Any proposed application the firm makes to court for the purposes of COBS TP 2.9B(1).</u>	<u>Sufficient notice to allow the FSA to make representations to the court.</u>

	<u>the FSA to make representations to the court.</u>			
--	--	--	--	--

Part 2: Comes into force on 31 March 2013

TP 2 Other Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provisions: coming into force
...					
2.9A	...				
2.9B	<u>COBS TP 2.9 and COBS TP 2.9A</u>	R	(1) Where a <i>firm</i> makes an application to court in relation to a <i>with-profits fund</i> to which, prior to the application to court, <u>COBS TP 2.9 and/or COBS 2.9A</u> applies, to the extent that <u>COBS TP 2.9 and/or COBS 2.9A</u> continues to be relevant, the <i>firm</i> must request that the court considers whether it is more appropriate for the <i>firm</i> to comply with the provisions in <u>COBS 20</u> applicable to TP 2.9 and/or 2.9A instead of the terms of the arrangement previously formally approved by the court, to the extent that the arrangement is inconsistent with those provisions.	31 March 2013 indefinitely	1 November 2007 and 31 July 2009

		<p><u>(2) A firm falling within (1) must provide the FSA with sufficient notice of any application it makes to court for the purposes of (1) in order to allow the appropriate regulator to make representations to the court.</u></p>		
--	--	--	--	--

Appendix 5

Linked long term insurance business

Annex A

Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

- collateral*
- (1) ...
- (2) (in *COBS* (except *COBS* 21.3) and *CASS*) any of the following:
...
- (3) (in *INSPRU*, *COBS* 21.3 and *SYSC*):
...
- permitted derivatives contract*
- in relation to *permitted links*, a contract involving a *derivative* or *quasi-derivative* that,
- (a) in the case of a *Solvency II undertaking*, satisfies *COBS* 21.3.13R to *COBS* 21.3.14G, as applied in relation to assets covering liabilities in respect of *linked long-term* contracts of insurance; and
- (b) in the case of *insurers* which are not *Solvency II undertakings*, satisfies *INSPRU* 3.2.5R to *INSPRU* 3.2.35AG with the exception of *INSPRU* 3.2.18R, as applied in relation to assets covering liabilities in respect of *linked long-term* contracts of insurance.
- permitted stock lending*
- in relation to *permitted links*, a *stock lending* transaction (including a *repo* transaction) that,
- (a) in the case of a *Solvency II undertaking*, satisfies *COBS* 21.3.11R to *COBS* 21.3.12R (inclusive); and
- (b) in the case of a *insurer* that is not a *Solvency II undertaking*, satisfies *INSPRU* 3.2.36AR to *INSPRU* 3.2.42G (inclusive).

Annex B

Amendments to the Conduct of Business sourcebook

Note to reader: Amendments proposed in this annex are to follow the draft Handbook text as consulted on in CP11/23 (Solvency II and linked long-term insurance business) and follows the numbering of the draft rules proposed in that Consultation Paper.

The following text is new and is not underlined.

21.3.9 R A *permitted stock lending* transaction is one which satisfies the requirements in COBS 21.3.11R to COBS 21.3.12R

21.3.10 G The specific method of *stock lending* permitted is an arrangement of the kind described in section 263B of the Taxation of Chargeable Gains Act 1992, under which the lender transfers *securities* to the borrower otherwise than by way of *sale* and the borrower is to transfer those *securities*, or *securities* of the same type and amount, back to the lender at a later date. In accordance with good market practice, a separate transaction by way of transfer of assets is also involved for the purpose of providing *collateral* to the "lender" to cover him against the risk that the future transfer back of the *securities* may not be satisfactorily completed.

Stock lending: requirements

- 21.3.11 R (1) The *stock lending* arrangement is of the kind described in section 263B of the Taxation of Chargeable Gains Act 1992 (without extension by section 263C), and:
- (a) all the terms of the agreement under which *securities* are to be reacquired by the *firm* for the account of the unit linked fund are in a form which is acceptable to the *firm* and are in accordance with good market practice;
 - (b) the counterparty is:
 - (i) an *authorised person*; or
 - (ii) a *person* authorised by a *Home State regulator*; or
 - (iii) a *person* registered as a broker-dealer with the Securities and Exchange Commission of the United States of America; or
 - (iv) a bank, or a branch of a bank, supervised and authorised to deal in investments as principal, with respect to *OTC derivatives*, by at least one of the following federal banking supervisory authorities of

the United States of America:

(A) the Office of the Comptroller of the Currency;

(B) the Federal Deposit Insurance Corporation;

(C) the Board of Governors of the Federal Reserve System; and

(D) the Office of Thrift Supervision; and

(c) *collateral* is obtained to secure the obligation of the counterparty under the terms referred to in (a) and the *collateral* is:

(i) acceptable to the *firm*;

(ii) adequate; and

(iii) sufficiently immediate; and

(d) for the purposes of *property-linked assets* only:

(i) where the *linked policyholder* bears the whole of the risk associated with the *stock lending* transaction, the *linked policyholder* receives the whole of the recompense (net of fees and expenses);

(ii) the extent of any risk that the *linked policyholder* bears in relation to the *stock lending* transaction is disclosed to them; and

(iii) where the risk associated with the *stock lending* transaction is borne outside the *linked fund*, the *linked fund* receives a fair and reasonable recompense for the use of the *linked policyholders'* funds.

(2) The counterparty for the purpose of (1) is the *person* who is obliged under the agreement referred to in (1)(a) to transfer to the *firm* the *securities* transferred by the *firm* under the *stock lending* arrangement or *securities* of the same kind.

(3) COBS 21.3.11R(1)(c) does not apply to a *stock lending* transaction made through Euroclear Bank SA/NV's Securities Lending and Borrowing Programme.

Stock lending: treatment of collateral

21.3.12 R (1) *Collateral* is adequate for the purposes of this section only if it is:

(a) transferred to the *firm*;

- (b) at least equal in value, at the time of the transfer to the *firm*, to the value of the *securities* transferred by the *firm*; and
- (c) in the form of one or more of:
 - (i) cash;
 - (ii) a certificate of *deposit*;
 - (iii) a letter of *credit*;
 - (iv) a *readily realisable security*;
 - (v) commercial paper with no embedded *derivative* content;
 - (vi) a *qualifying money market fund*.
- (2) *Collateral* is sufficiently immediate for the purposes of this section if:
 - (a) it is transferred before or at the time of the transfer of the *securities* by the *firm*; or
 - (b) the *firm* takes reasonable care to determine at the time referred to in (a) that it will be transferred at the latest by the close of business on the *day* of the transfer.
- (3) The *firm* must ensure that the value of the collateral at all times is at least equal to the value of the *securities* transferred by the *firm*.
- (4) The duty in (3) may be regarded as satisfied in respect of *collateral* the validity of which is about to expire or has expired where the *firm* takes reasonable care to determine that sufficient *collateral* will again be transferred at the latest by the close of business on the *day* of expiry.

Requirements for derivative contracts

- 21.3.13 R A *permitted derivatives contract* is one which is effected or issued:
 - (a) on or under the rules of a *regulated market*; or
 - (b) off-market with an *approved counterparty*.
- 21.3.14 G *Firms* are also required to comply with the prudent persons principle in SOLPRU 7 and ensure that the use of *derivative* contracts is adequately covered. *Firms* are also referred to the *rules* in COLL 5.3 (Derivative Exposure) in relation to the use of *derivatives* in investment funds and the further guidance from CESR and its successor body, ESMA, which represent good practice in this area.

Appendix 6

Consequential amendments to the Handbook

Annex A

Amendments to the Prudential sourcebook for Solvency II Insurers (SOLPRU)

Note to reader: All the text in this Annex is new text and is not underlined, with the exception of the deletion under SOLPRU 1 which is deleted with strikethrough text. All text follows chronologically from the text proposed for the new SOLPRU sourcebook within CP11/22.

1 Application and purpose

~~[Editorial note: text on the broad application and purpose of the sourcebook will be included in the second consultation paper on the *Solvency II Directive*, along with any further amendments to the individual application provisions already drafted at the beginning of each chapter.]~~

1.1 Application

- 1.1.1 G There is no overall application statement for *SOLPRU*. Each chapter or section has its own application statement. Broadly speaking however, *SOLPRU* applies to a *UK Solvency II firm*. In general terms *SOLPRU* also applies to Lloyd's by virtue of the application of various *SOLPRU* provisions to the *Society* and *managing agents*, such application provisions being located at the beginning of each *SOLPRU* chapter. In addition, *SOLPRU* 13 contains a series of provisions relevant to the application of the *Solvency II Directive* to Lloyd's.
- 1.1.2 R A *UK Solvency II firm* means a *firm* that satisfies the following conditions:
- (1) it is an *insurer*;
 - (2) its head office is in the *United Kingdom*;
 - (3) its *permission* does not include a *requirement* that the *firm* must only carry out *Solvency II excluded activities*;
 - (4) if it is a *Solvency I firm* it is not excluded pursuant to *SOLPRU* 1.1.6R;
 - (5) if it is a *non-Solvency I firm* it is not excluded pursuant to:
 - (i) *SOLPRU* 1.1.3R on the *SII implementation date*; or
 - (ii) *SOLPRU* 1.1.6R;
 - (6) if it obtains its *Part IV permission* for *effecting and carrying out contracts of insurance* on or after *SII implementation date* it is not excluded pursuant to:

- (i) *SOLPRU* 1.1.3R on the date it obtains such *Part IV permission*; or
 - (ii) *SOLPRU* 1.1.6R; and
- (7) it is not a *pure reinsurer* which had ceased to conduct new reinsurance contracts before 10 December 2007.
- 1.1.3 R A *firm* of the kind mentioned in *SOLPRU* 1.1.2R(5) or *SOLPRU* 1.1.2R(6) is excluded if it fulfils all of the following conditions:
- (1) the *firm's* annual gross written premium income does not exceed 5,000,000 euro;
 - (2) the total of the *firm's technical provisions*, gross of the amounts recoverable from *reinsurance contracts* and *ISPVs*, as referred to in *SOLPRU* 2.3 does not exceed 25,000,000 euro;
 - (3) where the *firm* belongs to a *insurance group*, the total of the *technical provisions* of the *group* defined as gross of the amounts recoverable from *reinsurance contracts* and *ISPVs* does not exceed 25,000,000 euro;
 - (4) the business of the *firm* does not include insurance or *reinsurance* activities covering liability, credit and suretyship insurance risks, unless they constitute *ancillary risks*; and
 - (5) the business of the *firm* does not include *reinsurance* operations:
 - (a) exceeding:
 - (i) 500,000 euro of its gross written premium income; or
 - (ii) 2,500,000 euro of its *technical provisions* gross of the amounts recoverable from *reinsurance contracts* and *ISPVs*; or
 - (b) with more than 10% of its gross written premium income or more than 10% of its *technical provisions* gross of the amounts recoverable from *reinsurance contracts* and *ISPVs*.
- 1.1.4 R A *firm* excluded under *SOLPRU* 1.1.3R shall cease to be excluded under that *rule* from the fourth year if any of the amounts set out in *SOLPRU* 1.1.3R(1), (2), (3) or (5) are exceeded in each of the three preceding years.
- 1.1.5 R A *firm* of the kind mentioned in *SOLPRU* 1.1.2R(6) is not excluded under *SOLPRU* 1.1.3R if any of the amounts set out in *SOLPRU* 1.1.3R(1), (2), (3) or (5) are expected to be exceeded within five years of the date the *firm* obtained its *Part IV permission* for *effecting and carrying out contracts of insurance*.

- 1.1.6 R Subject to *SOLPRU* 1.1.4R, a *firm* of the kind mentioned in *SOLPRU* 1.1.2R(4), (5) or (6) is excluded if:
- (1) the *firm* has not exercised passporting rights under the *Solvency II Directive*;
 - (2) the conditions in *SOLPRU* 1.1.3R(1) to (5):
 - (a) have not been breached for three consecutive years; and
 - (b) are not expected to be breached during the following five years.
- 1.1.7 G A *firm* is not excluded under *SOLPRU* 1.1.3R if its *Part IV permission* includes a *requirement* that it comply with the *rules* in *SOLPRU*.
- [**Note:** articles 4, 5(2), 7, 9(1), 9(2), 10(1) and 12 of the *Solvency II Directive*]
- 1.1.8 G Under article 300 of the *Solvency II Directive* the euro amounts specified in *SOLPRU* 1.1.4R are subject to review every five years. The relevant amounts will be increased by the percentage change in the Harmonised Indices of Consumer Prices (comprising all EU member states, as published by Eurostat) starting from [31 October 2012] until the date of revision and rounded up to a multiple of 100,000 euro, provided that where the percentage change since the previous revision is less than 5% the amounts will not be revised.

1.2 Purpose

- 1.2.1 G *SOLPRU* implements the majority of the new provisions in the *Solvency II Directive* and contains most of the prudential requirements for a *UK Solvency II firm* and Lloyd's. The precise provisions being implemented are listed as a note after each *rule*.
- 1.2.2 G *SOLPRU* is not a comprehensive sourcebook of all of the *rules* and *guidance* applicable to a *UK Solvency II firm* and Lloyd's in the *prudential context*. A *firm* should also refer to the application *rules* of other sourcebooks, for example *SYSC* and *SUP*, and should consider the application of sourcebooks in light of the *regulated activities* undertaken by the *firm*.
- 1.2.3 G *GENPRU* 3 applies to a *UK Solvency II firm* if it is a member of a *financial conglomerate*.
- 1.2.4 G [Placeholder for guidance on the process for implementing the exclusions envisaged above and for firms to opt into the *Solvency II regime*.]

2 Valuation

...

2.4 Calculation of technical provisions

...

General insurance business: Community co-insurance operations

- 2.4.18 R Where a *relevant insurer* determines the amount of a liability in order to make provision for outstanding *claims* under a *Community co-insurance operation*, if the *leading insurer* has informed the *relevant insurer* of the amount of the provision made by the *leading insurer* for such *claims*, the amount determined by the *relevant insurer*:
- (1) must be at least as great as the amount of the provision made by the *leading insurer*; or
 - (2) in a case where it is not the practice in the *United Kingdom* to make such provision separately, must be sufficient, when all liabilities are taken into account, to include provision at least as great as that made by the *leading insurer* for such *claims*,
- with due regard being had in either case to the proportion of the risk covered by the *relevant insurer* and by the *leading insurer* respectively.

[**Note:** article 192 of the *Solvency II Directive*]

3 Own funds

...

3.3 Classification and eligibility of own funds

...

3.3.13 G ...

Notification of issuance of own funds items

- 3.3.14 R *SOLPRU* 3.3.15R to *SOLPRU* 3.3.22G does not apply to the following:
- (1) any item which a *firm* intends to include within its *basic own funds* that is not covered by the list of *own funds* items set out in articles [] of the *Solvency II Regulation*, but which may be included in its *basic own funds* only if the *firm* has received the *FSA*'s approval; and
 - (2) any item which a *firm* intends to include within its *ancillary own funds*.
- 3.3.15 R A *firm* must notify the *FSA* in writing of its intention to issue an item which it intends to include within its *basic own funds* at least one *month* before the intended date of issue, unless there are exceptional circumstances which make it impracticable to give such a period of notice, in which event the *firm* must give as much notice as it practicable in those circumstances.

When giving notice, a *firm* must:

- (1) provide details of the amount of *basic own funds* the *firm* is seeking to raise through the intended issue and whether the own funds is intended to be issued to external investors or within its *group*;
- (2) identify the classification of *basic own funds* the item is intended to fall within;
- (3) include confirmation from the *governing body* of the *firm* that the item complies with the *rules* applicable to items of *basic own funds* included in the classification of the item identified in (2); and
- (4) provide a copy of the term sheet and details of any features of the item it intends to include within its *basic own funds* which are novel, unusual or different from an item of *basic own funds* of a similar nature previously issued by the *firm* or widely available in the market or not specifically contemplated by *SOLPRU* or the *Solvency II Regulation*.

3.3.16 R A *firm* must provide a further written notification to the *FSA* including all the information required in *SOLPRU* 3.3.15R(1) to (4) as soon as it proposes any change to the intended date of issue, amount of issue, type of investors, classification of a particular tier of *basic own funds* or any other feature of the item intended to be included as *basic own funds* to that previously notified to the *FSA*.

3.3.17 R If a *firm* proposes to establish a debt securities program for the issue of an item for inclusion within its *basic own funds*, it must:

- (1) notify the *FSA* of the establishment of the program; and
- (2) provide the information required by *SOLPRU* 3.3.15R(1) to (4)

at least one *month* before the first proposed drawdown. The *FSA* must be notified of any changes in accordance with *SOLPRU* 3.3.16R.

3.3.18 R The items of *basic own funds* to which *SOLPRU* 3.3.15R does not apply are:

- (1) ordinary *shares* which:
 - (a) meet the classification criteria for ordinary share capital in *Tier 1 own funds*; and
 - (b) are the same as ordinary *shares* previously issued by the *firm*;
- (2) debt instruments issued from a debt securities program, provided that program was notified to the *FSA* prior to its first drawdown, in accordance with *SOLPRU* 3.3.17R; and
- (3) any item which is not materially different in terms of its characteristics and eligibility for inclusion in a particular tier of *basic*

own funds to items previously issued by the *firm* and included in *basic own funds*.

- 3.3.19 G For the purposes of SOLPRU 3.3.18R(1)(a), a *firm* must assess whether the item of *basic own funds* satisfies all relevant criteria for classification as ordinary share capital in *Tier 1 own funds*. For example, the *firm* must assess whether the *basic own funds* items rank after all other claims including other classes of share capital in the event the *firm* is wound up.
- 3.3.20 R A *firm* must notify the *FSA* in writing, no later than the date of issue, of its intention to issue an item listed in SOLPRU 3.3.18R which it intends to include within its *basic own funds*. When giving notice, a *firm* must:
- (1) provide the information set out at SOLPRU 3.3.15R(1) to (3); and
 - (2) confirm that the terms of the item have not changed since the previous issue by the *firm* of that type of item of *basic own funds*.
- 3.3.21 G SOLPRU 3.3.15R provides that, in exceptional circumstances, a *firm* may provide less than one *month's* notice of the intended issue. The *FSA* is unlikely to consider circumstances to be exceptional unless they are such that there is a risk of a *firm* not complying with its *SCR* or, as the case may be, *MCR* if a one-*month* notification period is observed. In such circumstances, a *firm* should notify the *FSA* as soon as it has resolved to issue further items it intends to include as *basic own funds*, and provide details of its circumstances and why it is not possible to provide one *month's* notice of the intended issue.
- 3.3.22 G Details of the notification to be provided by a *firm* in relation to items of *basic own funds* issued by another *undertaking* in its *group* for inclusion in its *own funds* are set out in SOLPRU 11.3.11R to SOLPRU 11.3.16R.

...

9 Conditions governing business

...

9.11 Restriction of business

- 9.11.1 R (1) A *firm* other than a *pure reinsurer* must not carry on any commercial business other than *insurance business* and activities directly arising from that business.
- (2) (1) does not prevent a *friendly society* which was on 15 March 1979 carrying on *long-term insurance business* from continuing to carry on savings business.

[Note: articles 18(1)(a) and 305(3) of the *Solvency II Directive*]

- 9.11.2 R A *pure reinsurer* must not carry on any business other than the business of

reinsurance and related operations.

[**Note:** articles 18(1)(a) and 305(3) of the *Solvency II Directive*]

- 9.11.3 R In *SOLPRU* 9.11.2R related operations include, for example, activities such as provision of statistical or actuarial advice, risk analysis or research for its clients. It may also include a *holding company* function and activities with respect to financial sector activities within the meaning of Article 2, point 8, of the *Financial Groups Directive*. But it does not allow the carrying on of, for example, unrelated banking and financial activities.

[**Note:** article 18(1)(b) of the *Solvency II Directive*]

9.12 Premiums for new business

- 9.12.1 R A *firm* must not enter into a *long-term insurance contract* unless it is satisfied, on reasonable actuarial assumptions, that the *premiums* receivable shall be sufficient:

- (1) to enable the *firm* to meet all of its *commitments*; and
- (2) in particular, to establish adequate technical provisions as required by *SOLPRU* 2.3.1R

[**Note:** article 209 of the *Solvency II Directive*]

- 9.12.2 R For the purposes of *SOLPRU* 9.12.1R, all aspects of the financial situation of the *firm* may be taken into account, provided that input from resources other than *premiums* and investment income expected to be earned from *premiums* is not systematic and permanent in a way that may jeopardise the long term solvency of the *firm*.

[**Note:** article 209 of the *Solvency II Directive*]

...

11 Group supervision

...

11.3 Group solvency: general provisions

...

- 11.3.10 R ...

- 11.3.11 R This section applies to a *firm* if another member of its *group* intends to issue an item for inclusion within the *basic own funds* forming the *own funds eligible for the group SCR* of the *firm's insurance group*.

- 11.3.12 R A *firm* must notify the *FSA* in writing of the intention of another member of its *group* which is not a *firm* to issue an item which it intends to include

within the *basic own funds* forming the *own funds eligible for the group SCR*, as soon as it becomes aware of the intention of the *group undertaking*. When giving notice, a *firm* must:

- (1) provide details of the amount of *basic own funds* to be raised through the intended issue and whether the item is intended to be issued to external investors or within its *group*;
- (2) identify the classification of *basic own funds* the item is intended to fall within;
- (3) include confirmation from the *governing body* of the *firm* that the item complies with the *rules* applicable to items of *basic own funds* included in the classification of the item identified in (2); and
- (4) provide a copy of the term sheet and details of any features of the item it intends to include within the *basic own funds* forming the *own funds eligible for the group SCR* which are novel, unusual or different from an item of *own funds* of a similar nature previously issued by the *firm* or widely available in the market or not specifically contemplated by *SOLPRU* or the *Solvency II Regulation*.

11.3.13 R A *firm* must provide a further written notification to the *FSA* including all the information required in *SOLPRU* 11.3.12R(1) to (4) as soon as it proposes any change to the intended date of issue, amount of issue, type of investors, classification of a particular tier of *basic own funds* or any other feature of the item intended to be included as *basic own funds* to that previously notified to the *FSA*.

11.3.14 R If a *group undertaking* proposes to establish a debt securities program for the issue of an item which the *firm* intends to include within the *basic own funds* forming the *own funds eligible for the group SCR*, it must:

- (1) notify the *FSA* of the establishment of the program; and
- (2) provide the information required by *SOLPRU* 11.3.12R(1) to (4)

as soon it becomes aware of the proposed establishment. The *FSA* must be notified of any changes in accordance with *SOLPRU* 11.3.13R.

11.3.15 R The items of *basic own funds* to which *SOLPRU* 11.3.12R does not apply are:

- (1) ordinary *shares* issued by a *group undertaking* which are:
 - (a) classified as *Tier 1 own funds* or *Tier 2 basic own funds*; and
 - (b) the same as ordinary *shares* previously issued by the *group undertaking*;
- (2) debt instruments issued from a debt securities program established by the *group undertaking*, provided that program was notified to the

FSA prior to its first drawdown in accordance with *SOLPRU* 11.3.14R; and

- (3) any item which is not materially different in terms of its characteristics and eligibility for inclusion in a particular tier of *basic own funds* to items previously issued by the *group undertaking* and included in the *basic own funds* forming the *own funds eligible for the group SCR*.

11.3.16 R A *firm* must notify the *FSA* in writing, no later than the date of issue, of the intention of the *group undertaking* to issue an item listed in *SOLPRU* 11.3.15R which it intends to include within the *basic own funds* forming the *own funds eligible for the group SCR*. When giving notice, a *firm* must:

- (1) provide the information set out at *SOLPRU* 11.3.12R(1) to (3); and
- (2) confirm that the terms of the item have not changed since the previous issue of that type of item of *basic own funds* by that *group undertaking*.

...

Schedules

...

Sch 2 Notification and reporting requirements

...

Handbook reference	Matter to be notified	Contents of notification	Trigger events	Time allowed
<i>SOLPRU</i> 2.4.16R	...	...	...	...
...				
<i>SOLPRU</i> 3.3.15R	Intention to issue an item for inclusion within <i>basic own funds</i>	Fact of intention and details of intended amount, issue date, type of investor, classification intended, features of instrument and confirmation of compliance with <i>rules</i>	Intention to issue	One <i>month</i> prior to issue, unless exceptional circumstances prevent a <i>firm</i> adhering to a one-month period
<i>SOLPRU</i> 3.3.16R	Proposed changes to details of the	Proposed change and all information required under <i>SOLPRU</i>	Intention to change any details of the	As soon as the changes are

	issue of an item of <i>basic own funds</i> notified under <i>SOLPRU</i> 3.3.15R	3.3.15R(1) to (4)	issue previously notified to the <i>FSA</i>	proposed
<i>SOLPRU</i> 3.3.17R	Proposed establishment of a debt securities program	All information required under <i>SOLPRU</i> 3.3.15R(1) to (4)	Intention to establish	One <i>month</i> prior to first drawdown
<i>SOLPRU</i> 3.3.20R	Issue of an item of <i>basic own funds</i> where the item or facility previously notified to the <i>FSA</i>	All information required under <i>SOLPRU</i> 3.3.15R(1) to (3) and confirmation no changes have been made to the terms of the item of <i>basic own funds</i> since a previous similar issue	Intention to issue	No later than date of issue
...				
<i>SOLPRU</i> 11.3.10R (3)	...	...	...	...
<i>SOLPRU</i> 11.3.12R	Intention of a <i>group undertaking</i> to issue an item for inclusion within <i>basic own funds</i> forming the <i>own funds eligible for the group SCR</i>	Fact of intention and details of intended amount, issue date, type of investor, classification intended, features of instrument and confirmation of compliance with <i>rules</i>	Intention to issue	As soon as proposed issue becomes known to <i>firm</i>
<i>SOLPRU</i> 11.3.13R	Proposed changes to details of the issue of an item of <i>basic own funds</i> notified under <i>SOLPRU</i> 11.3.11R	Proposed change and all information required under <i>SOLPRU</i> 11.3.12R(1) to (4)	Intention to change any details of the issue previously notified to the <i>FSA</i>	As soon as the changes are proposed
<i>SOLPRU</i>	Proposed	All information required	Intention to	As soon as

11.3.14R	establishment of a debt securities program by a <i>group undertaking</i>	under <i>SOLPRU</i> 11.3.12R(1) to (4)	establish	proposed establishment becomes known to <i>firm</i>
<i>SOLPRU</i> 11.3.16R	Issue of an item of <i>basic own funds</i> by a <i>group undertaking</i> where the item or facility previously notified to the <i>FSA</i>	All information required under <i>SOLPRU</i> 11.3.12R(1) to (3) and confirmation no changes have been made to the terms of the item of <i>basic own funds</i> since a previous similar issue	Intention to issue	No later than date of issue
<i>SOLPRU</i> 11.7.4R(2) (a)	...	...	...	...
...				

Annex B

Amendments to Glossary definitions

Note to reader: Some of the italicised terms are new Glossary definitions related to, or used in, the proposed version of the Prudential sourcebook for Solvency II Insurers (SOLPRU) in CP11/22 (Transposition of Solvency II) which have not been made. The Glossary terms marked with “*” are those which CP11/22 has proposed to amend; however, the amendment shown below supersedes that proposed amendment.

In this section, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

<i>admissible asset</i>	<p>(1) (for the purpose of the rules in GENPRU and INSPRU as they apply to members of the Society of Lloyd's, the Society and managing agents) an asset that, subject to paragraphs (2) and (3) of GENPRU 2 Annex 7R, falls into one or more categories in paragraph (1) of GENPRU 2 Annex 7R as modified by GENPRU 2.3.34R.</p> <p>(2) otherwise:</p> <p>(a) (in relation to an <i>insurer</i> which is not a <i>pure reinsurer</i>) an asset that, subject to paragraphs (2) and (3) of GENPRU 2 Annex 7R, falls into one or more categories in paragraph (1) of GENPRU 2 Annex 7R; or</p> <p>(b) (in relation to a <i>pure reinsurer</i>) an asset the holding of which is consistent with compliance by the <i>firm</i> with INSPRU 3.1.61AR.</p>
<i>ancillary risk</i>	(in relation to an <i>insurer</i> with <i>permission</i> under the <i>Act</i> to insure a principal risk belonging to one <i>class</i> (as defined for the purposes of INSPRU, SOLPRU and SUP) of <i>general insurance business</i>) a risk included in another such class ...
<i>annualised net written premiums</i>	<p>(for the purposes of INSPRU 1.4) in relation to a <i>financial year</i>, the net written premiums received during that <i>financial year</i>, except that in relation to a financial annualised net written premiums year that has been validly extended beyond, or shortened from, a period of 12 months, the amount of <i>net written premiums</i> is the amount determined in accordance with the formula: $NWP \times 365/D$ where:</p> <p>(1) NWP is the amount of <i>net written premiums</i> received in the <i>financial year</i>; and</p> <p>(2) D is the number of days in that <i>financial year</i>.[deleted]</p>

<i>assessable mutual</i>	(for the purposes of <i>INSPRU</i> 1.4) a <i>mutual</i> where the <i>insurance business</i> carried on by the <i>mutual</i> is limited to the provision of <i>insurance business</i> to its members and whose articles of association, rules or bye-laws provide for the calling of additional contributions from members to meet <i>claims</i> .
<i>balancing amount</i>	in respect of a <i>syndicate</i> , any part of the <i>capital resources</i> that: (a) the <i>managing agent</i> of the <i>syndicate</i> has assessed to be necessary to support the <i>insurance business</i> carried on by the <i>members</i> of the <i>syndicate</i> through the <i>syndicate</i>, including those <i>capital resources</i> required to support the risks arising at <i>syndicate</i> level that affect that business; but (b) are not managed by or at the direction of the <i>managing agent</i> of the <i>syndicate</i> . [deleted]
<i>capital instrument</i>	(in <i>GENPRU</i> , <u>and</u> <i>BIPRU</i> and <i>INSPRU</i> 6 and in relation to an <i>undertaking</i>) any <i>security</i> issued by or loan made to that <i>undertaking</i> or any other investment in, or external contribution to the capital of, that <i>undertaking</i> .
<i>collective insurance</i>	(in relation to a <i>class of contract of insurance</i>) the <i>class of contract of insurance</i> , specified in paragraph VIII of Part II of Schedule 1 to the <i>Regulated Activities Order</i> (Contracts of long-term insurance), of a kind referred to in article 2(2)(e) of the <i>Consolidated Life Directive</i> 2(3)(b)(v) of the <i>Solvency II Directive</i> ("the operations carried out by <u>life insurance undertakings</u> companies such as those referred to in Chapter 1, Title 4 of Book IV of the French "Code des assurances").
<i>commitment</i>	a commitment represented by <i>insurance business</i> of any of the <i>classes</i> (as defined for the purposes of <i>INSPRU</i> , <i>SOLPRU</i> and <i>SUP</i>) of <i>long-term insurance business</i> .
<i>Community Co-Insurance Directive</i>	the Council Directive of 30 May 1978 on the coordination of laws, regulations and administrative provisions relating to Community co-insurance (No 78/473/EEC). [deleted]
<i>community co-insurance operation</i>	an operation to which <u>articles 190 to 196 of the <i>Solvency II Directive</i></u> apply the <i>Community Co-Insurance Directive</i> applies, as modified by article 26 <i>Second Non-Life Directive</i>.
<i>competent authority</i>	... (3) (in relation to a group, and for the purposes of <i>SYSC</i> 12 (Group risk systems and controls requirement), <i>GENPRU</i> , <u>and</u> <i>BIPRU</i> and <i>INSPRU</i> , any national authority of an <i>EEA State</i> which is empowered by law or regulation to supervise <i>regulated entities</i> , whether on an individual or group-wide basis.

	...
<i>Consolidated Life Directive</i>	the Council Directive of 5 November 2002 on the taking-up and pursuit of the business of life assurance (No 2002/83/EC), which consolidates the provisions of the <i>First, Second and Third Life Directives</i>.
<i>counterparty</i>	(1) (in <i>UPRU</i>) any person with or for whom a firm carries on <i>designated investment business</i> or an <i>ancillary activity</i> . (2) for the purposes of the rules relating to insurers in <i>GENPRU</i> and <i>INSPRU</i>) (in relation to an <i>insurer</i>, the <i>Society</i>, a <i>syndicate</i> or <i>member</i> ('A²')): ...
<i>covered bond</i>	... (4) (in accordance with Article 22(4) of the <i>Third Non-Life Directive</i> and Article 24(4) of the <i>Consolidated Life Directive</i> and for the purposes of <i>INSPRU</i> 2.1) a <i>debenture</i> that is issued by a <i>credit institution</i> ...
<i>credit equalisation provision</i>	the provision required to be established by <i>INSPRU</i> 1.4.43R. [deleted]
<i>EEA insurer*</i>	an <i>insurer</i> , other than a <i>pure reinsurer</i> or a <i>non-directive insurer</i> , whose head office is in any <i>EEA State</i> except the <i>United Kingdom</i> and which has received <i>authorisation</i> under article 6 of the <i>First Life Directive</i> or article 4 of the <i>Consolidated Life Directive</i> or article 6 of the <i>First Non-Life Directive</i> <u>article 14 of the <i>Solvency II Directive</i></u> from its <i>Home State Regulator</i> <u><i>regulator</i></u> .
<i>EEA prudential sectoral legislation</i>	... (b) (in relation to the <i>insurance sector</i>) in particular this includes requirements laid down in the <i>First Non-Life Directive</i>, the <i>Consolidated Life Directive</i> and the <i>Insurance Groups Directive</i> <u><i>Solvency II Directive</i></u> .
<i>EEA pure reinsurer</i>	a <i>reinsurance undertaking</i> (other than an <i>ISPI</i>) <u><i>pure reinsurer</i></u> whose head office is in any <i>EEA State</i> except the <i>United Kingdom</i> and which has received (or is deemed to have received) authorisation under article 3 of the <i>Reinsurance Directive</i> <u>article 14 of the <i>Solvency II Directive</i></u> from its <i>Home State Regulator</i> <u><i>regulator</i></u> .
<i>EEA regulated entity</i>	(1) (except in <i>GENPRU</i> 3) a <i>regulated entity</i> that is an <i>EEA firm</i> or a <i>UK firm</i> .

	(2) <u>(in GENPRU 3) a regulated entity that is an EEA firm or a UK firm but, in the case of an insurance undertaking, excluding any firm which is not a Solvency II undertaking.</u>
<i>equalisation provision</i>	a provision required to be established under the rules in INSPRU 1.4. [deleted]
<i>financial year in question</i>	(for the purposes of INSPRU 1.1 and of the definition of non-directive insurer) the last <i>financial year</i> to end before the date on which the latest accounts of the <i>insurer</i> are required to be deposited with the <i>FSA</i> ; the preceding <i>financial year</i> and previous <i>financial years</i> are construed accordingly.
<i>First Life Directive</i>	the Council Directive of 5 March 1979 on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of direct life assurance (No 79/267/EEC). [deleted]
<i>group capital resources</i>	in relation to an undertaking in INSPRU 6.1.17R, that undertaking's group capital resources as calculated in accordance with INSPRU 6.1.36R. [deleted]
<i>group capital resources requirement</i>	in relation to an undertaking in INSPRU 6.1.17R, that undertaking's group capital resources requirement as calculated in accordance with INSPRU 6.1.33R. [deleted]
<i>IMD insurance undertaking</i>	(as defined in article 2(1) of the <i>Insurance Mediation Directive</i>) an undertaking which has received official authorisation in accordance with article 6 14 of the Consolidated Life Directive or article 6 of the First Non-Life Directive Solvency II Directive.
<i>insurance business grouping</i>	a grouping comprising descriptions of general insurance business determined in accordance with INSPRU 1.4.12R. [deleted]
<i>Insurance Groups Directive</i>	Directive of the European Parliament and of the Council of 27 October 1998 on the supplementary supervision of insurance undertakings in an insurance group (1998/78/EC). [deleted]
<i>insurance undertaking</i>	(1) (except in COBS) an undertaking, or (in CASS 5 and COMP) a member, whether or not an insurer, which carries on insurance business. (2) (in COBS) an undertaking or a member which carries on insurance business. <u>an undertaking, whether or not an insurer, including a member which carries on insurance business.</u>
<i>internal controls</i>	(1) <u>(except in SOLPRU and generally in relation to a UK Solvency II firm, the Society and managing agents), the whole system of controls, financial or otherwise, established by the management of a firm in order to:</u>

- (a) carry on the business of the *firm* in an orderly and efficient manner;
- (b) ensure adherence to management policies;
- (c) safeguard the assets of the *firm* and other assets for which the *firm* is responsible; and
- (d) secure as far as possible the completeness and accuracy of the *firm's* records (including those necessary to ensure continuous compliance with the requirements or standards under the *regulatory system* relating to the adequacy of the *firm's* financial resources).

(2) (in SOLPRU and generally in relation to a UK Solvency II firm, the Society and managing agents) the internal control system and other requirements which apply under SOLPRU 9.4.1R to 9.4.4R.

<i>leading insurer</i>	(in relation to a <i>community co-insurance operation</i>) has the same meaning as in <u>used for the purposes of articles 190 to 196 of the Community Co-Insurance Solvency II Directive.</u>
<i>Lloyd's actuary</i>	the actuary appointed by the Society under SUP 4.6.1R. [deleted]
<i>Lloyd's actuary function</i>	controlled function CF12B in the table of controlled functions, described more fully in SUP 10.7.22 R. [deleted]
<i>Lloyd's Return</i>	the financial report that the Society is required to submit to the FSA under IPRU(INS) 9.48(1). [deleted]
<i>material outsourcing</i>	<p>(1) <u>except in relation to a UK Solvency II firm, the Society and managing agents, outsourcing services of such importance that weakness, or failure, of the services would cast serious doubt upon the firm's continuing satisfaction of the threshold conditions or compliance with the Principles.</u></p> <p>(2) <u>in relation to a UK Solvency II firm, the Society and managing agents, outsourcing services in relation to obligations under the Solvency II Directive or in relation to functions to which Article 49 of that directive applies.</u></p>
<i>non-credit equalisation provision</i>	the provision required to be established under INSPRU 1.4.17R. [deleted]
<i>non-directive firm</i>	<p>(in SUP 11 (Controllers and close links) and SUP 16 (Reporting requirements)) ...</p> <p>(d) <u>a Solvency II undertaking, the Society and managing agents an undertaking pursuing the activity of direct insurance within the</u></p>

meaning of:

(i) article 2 of the *Consolidated Life Directive*, authorised under that directive; or

(ii) article 1 of the *First Non-Life Directive*, authorised under that directive;

(e) an *undertaking* pursuing the activity of *reinsurance* within the meaning of article 2.1 (a) of the *Reinsurance Directive*, authorised under that directive.

non-directive friendly society

(a) a *friendly society* whose *insurance business* is restricted to the provision of benefits which vary according to the resources available and in which the contributions of the members are determined on a flat rate basis;

(b) a *friendly society* whose *long term insurance business* is restricted to the provision of benefits for employed and self-employed *persons* belonging to an undertaking or group of undertakings, or a trade or group of trades, in the event of death or survival or of discontinuance or curtailment of activity (whether or not the commitments arising from such operations are fully covered at all times by mathematical reserves);

(c) a *friendly society* which undertakes to provide benefits solely in the event of death where the amount of such benefits does not exceed the average funeral costs for a single death or where the benefits are provided in kind;

(d) a *friendly society* (carrying on *long term insurance business*):

(i) whose registered rules contain provisions for calling up additional contributions from members or reducing their benefits or claiming assistance from other *persons* who have undertaken to provide it; and

(ii) whose annual gross premium income (other than from contracts of reinsurance) has not exceeded 5 million Euro for each of the three preceding financial years;

(e) a *friendly society* (carrying on *general insurance business*):

(i) whose registered rules contain provisions for calling up additional contributions from members or reducing their benefits;

(ii) whose gross premium income (other than from contracts of reinsurance) for the preceding financial year did not exceed 5 million Euro; and

(iii) whose members provided at least half of that gross premium income;

(f)

(i) a *friendly society* whose liabilities in respect of *general insurance contracts* are fully reinsured with or guaranteed by other *mutuals* (including *friendly societies*); and

~~(ii) the *mutuals* providing the *reinsurance* or the *guarantee* are subject to the rules of the *First Non-Life Directive*;~~

~~and in each case whose *insurance business* is limited to that described in any of (a) to (f).~~

~~a *friendly society* that is not a *UK Solvency II firm*.~~

non-directive insurer

~~(a) an *insurer* which is a provident or mutual benefit institution whose *insurance business* is restricted to the provision of benefits which vary according to the resources available and in which the contributions are determined on a flat-rate basis; or~~

~~(b) an *insurer* whose *long-term insurance business* is restricted to the provision of benefits for employed and self-employed persons belonging to an *undertaking* or group of *undertakings*, or a trade or group of trades, in the event of death or survival or of discontinuance or curtailment of activity (whether or not the commitments arising from such operations are fully covered at all times by mathematical reserves); or~~

~~(c) an *insurer* which undertakes to provide benefits solely in the event of death where the amount of such benefits does not exceed the average funeral costs for a single death or where the benefits are provided in kind; or~~

~~(d) a *mutual* (carrying on *long-term insurance business*) whose:~~

~~(i) articles of association contain provisions for calling up additional contributions from members or reducing their benefits or claiming assistance from other persons who have undertaken to provide it; and~~

~~(ii) annual gross *premium* income (other than from contracts of *reinsurance*) has not exceeded 5 million Euro for each of the *financial year* in question and the two previous *financial years*; or~~

~~(e) a *mutual* (carrying on *general insurance business*) whose:~~

~~(i) articles of association contain provisions for calling up additional contributions from members or reducing their benefits;~~

~~(ii) business does not cover liability risks, other than *ancillary risks*, or credit or suretyship risks;~~

~~(iii) gross *premium* income (other than from contracts of *reinsurance*) for the *financial year in question* did not exceed 5 million Euro; and~~

~~(iv) members provided at least half of that gross *premium* income; or~~

~~(f) an *insurer* whose *insurance business* (other than *reinsurance*) is:~~

~~(i) restricted to the provision of assistance for persons who get into difficulties while travelling, while away from home or while away from their permanent residence;~~

	<p>(ii) carried out exclusively on a local basis and consists only of benefits in kind; and</p> <p>(iii) such that the gross <i>premium</i> income from the provision of assistance in the <i>financial year in question</i> did not exceed 200,000 Euro; or</p> <p>(g)</p> <p>(i) a <i>mutual</i> whose liabilities in respect of <i>general insurance contracts</i> are fully reinsured with or guaranteed by other <i>mutuals</i> (including <i>friendly societies</i>); and</p> <p>(ii) the <i>mutuals</i> providing the <i>reinsurance</i> or the guarantee are subject to the rules of the <i>First Non-Life Directive</i>. [deleted]</p>
<i>non-directive mutual</i>	a <i>mutual</i> that falls into (d), (e) or (g) of the definition of a <i>non-directive insurer</i> <u>which is not a <i>Solvency II undertaking</i> or the <i>Society</i>.</u>
<i>Non-Life Directives</i>	the <i>First Non-Life Directive</i>, the <i>Second Non-Life Directive</i> and the <i>Third Non-Life Directive</i>. [deleted]
<i>non-Solvency I firm*</i>	a <i>firm</i> that immediately before the <i>Solvency II implementation date</i> was a <i>non-directive firm</i> <u>fell outside the scope of the <i>Solvency I Directive</i>.</u>
<i>participating insurance undertaking</i>	<p>an insurer which:</p> <p>(a) has a <i>subsidiary undertaking</i> that is an <i>insurance undertaking</i>;</p> <p>or</p> <p>(b) holds a <i>participation</i> in an <i>insurance undertaking</i>; or</p> <p>(c) is linked to an <i>insurance undertaking</i> by a <i>consolidation Article 12(1) relationship</i>. [deleted]</p>
<i>participation</i>	<p>(for the purposes of <i>UPRU</i> and <i>GENPRU</i> and for the purposes of <i>BIPRU</i> and <i>INSPRU</i> as they apply <u>as it applies</u> on a consolidated basis):</p> <p>...</p>
<i>receivable</i>	(in relation to a <i>member</i> , a period and a <i>premium</i>) a <i>premium</i> due to the <i>member</i> in respect of <i>contracts of insurance</i> effected during the period, whether or not the <i>premium</i> is received during that period. [deleted]
<i>regulated insurance entity</i>	an insurance undertaking <u>or reinsurance undertaking</u> within the meaning of Article 4 of the <i>Consolidated Life Directive</i> , Article 6 of the <i>First Non-Life Directive</i> or Article 1(b) of the <i>Insurance Groups Directive</i> article 13(1) of the <i>Solvency II Directive</i> .
<i>Second Life Directive</i>	the Council Directive of 8 November 1990 on the coordination of laws, etc and laying down provisions relating to facilitate the effective exercise of freedom to provide services and amending

	Directive 79/267/EEC (No 90/619/EEC). [deleted]
<i>sectoral rules</i>	(in relation to a <i>financial sector</i>) rules and requirements relating to the prudential supervision of <i>regulated entities</i> applicable to <i>regulated entities</i> in that <i>financial sector</i> as follows: ... (f) (in relation to any <i>financial sector</i>) those requirements include both ones applying on a solo basis and ones applying on a consolidated basis; <u>and</u> (g) (in relation to the <i>insurance sector</i>) references in this definition to consolidated supervision are to supplementary supervision, similar expressions being interpreted accordingly; and [deleted] ...
<i>Single Market Directives</i>	(a) the <i>Banking Consolidation Directive</i> ; (b) the <i>Solvency II Directive</i> Insurance Directives (within the meaning of paragraph 1 of Schedule 3 to the Act); (ba) the <i>Reinsurance Directive</i> ; (c) <i>MiFID</i> ; (d) the <i>Insurance Mediation Directive</i> ; and (e) the <i>UCITS Directive</i> .
<i>social insurance</i>	(in relation to a <i>class of contract of insurance</i>) the <i>class of contract of insurance</i> , specified in paragraph IX of Part II of Schedule 1 to the <i>Regulated Activities Order</i> (Contracts of long-term insurance), of a kind referred to in article 2(3)(c) of the <i>Consolidated Life Directive</i> <i>Solvency II Directive</i> ("operations relating to the length of human life which are prescribed by or provided for in <i>social insurance</i> legislation, <u>when in so far as they are effected or managed by life insurance undertakings</u> at their own risk by assurance undertakings in accordance with the laws of an <i>EEA State</i> ").
<i>Society GICR</i>	the <i>general insurance capital requirement</i> calculated by the <i>Society</i> as if it were an <i>insurer</i> under <i>GENPRU 2.3.13R</i>. [deleted]
<i>solo capital resources</i>	(1) (for the purposes of <i>GENPRU 3</i> and <i>INSPRU 6</i>) capital resources <u>or eligible own funds</u> that are or would be eligible as capital under the <i>sectoral rules</i> that apply for the purpose of calculating its <i>solo capital resources requirement</i> . Paragraph 6.8 of <i>GENPRU 3 Annex 1R</i> (Solo capital resources requirement: the insurance sector) applies for the purpose of this definition in the same way as it does for the definition of <i>solo capital resources requirement</i> . (2) ...

solo capital resources requirement (1) ...

(2) (for the purposes of ~~INSPRU 6~~ GENPRU 1) a capital resources requirement calculated on a solo basis as defined in paragraph 6.2 to 6.7 of GENPRU 3 Annex 1R as it would apply if references to *financial conglomerate* in those paragraphs were replaced with references to *insurance group*.

(3) ...

*Solvency I Directive** ~~the Directive of the European Parliament and of the Council of 5 March 2002 amending Council Directive 79/267/EEC as regards the solvency margin requirements for life assurance undertakings (No. 2002/12/EC)~~

each of:

(a) the Consolidated Life Directive;

(b) the First Non-Life Directive;

(c) the Second Non-Life Directive;

(d) the Third Non-Life Directive; and

(e) the Reinsurance Directive.

Solvency II excluded activities

(a) a mutual whose insurance business is restricted to the provision of benefits which vary according to the resources available and in which the contributions of the members are determined on a flat-rate basis;

(b) a mutual whose liabilities in respect of general insurance contracts must be fully reinsured with or guaranteed by other mutuals (including friendly societies) and the mutuals providing the reinsurance or the guarantees are Solvency II undertakings;

(c) an insurer whose long-term insurance business is restricted to the provision of benefits for employed and self-employed persons belonging to an undertaking or group of undertakings, or a trade or group of trades, in the event of death or survival or of discontinuance or curtailment of activity (whether or not the commitments arising from such operations are fully covered at all times by mathematical reserves); or

(d) an insurer whose insurance business restricted to the provision of benefits solely in the event of death where the amount of such benefits does not exceed the average funeral costs for a single death or where the benefits are provided in kind.

State of the commitment

... in this definition, "commitment" means (in accordance with article 2 of the Financial Services and Markets Act 2000 (Control of Business Transfers) (Requirements on Applicants) Regulations 2001 (SI 2001/3625)) any contract of insurance of a kind referred

	to in article 2 of the Consolidated Life Directive <u>article 2(3) of the Solvency II Directive.</u>
<i>syndicate actuary</i>	an actuary appointed to a syndicate as required by SUP 4.6.9R(1). [deleted]
<i>syndicate ICA</i>	the capital assessment performed by a managing agent under the overall Pillar 2 rule, GENPRU 1.5.1R(1), INSPRU 7.1 and INSPRU 1.1.57R(1) in respect of each syndicate managed by it. [deleted]
<i>Third Life Directive</i>	the Council Directive of 10 November 1992 on the coordination of laws, etc, and amending Directives 79/267/EEC and 90/619/EEC (No 92/96/EEC). [deleted]
<i>UK insurer</i>	an insurer, other than a UK Solvency II firm which is not a pure reinsurer or a non-directive insurer, whose head office is in the United Kingdom. [deleted]
<i>UK Solvency II firm*</i>	a firm that satisfies the following conditions: <ul style="list-style-type: none"> (1) it is an insurer; (2) its head office is in the United Kingdom; (3) if it is a Solvency I firm, it is not excluded pursuant to [rules transposing article 4(4) of the Solvency II Directive]; (4) if it is a non-Solvency I firm, either: <ul style="list-style-type: none"> (a) it is excluded pursuant to [rules transposing article 4(1) (3) of the Solvency II Directive] but it has opted to be a Solvency II undertaking pursuant to [rules/mechanics to opt in]; or (b) it is not excluded pursuant to [rules transposing article 4(1) (3) of the Solvency II Directive]; and (5) if it is neither a Solvency I firm nor a non-Solvency I firm, either: <ul style="list-style-type: none"> (a) it is excluded pursuant to [rules transposing article 4(1) (3) of the Solvency II Directive] but it has opted to be a Solvency II undertaking pursuant to [rules/mechanics to opt in]; or (b) it is not excluded pursuant to [rules transposing article 4(1) (3) of the Solvency II Directive]. <p><u>a firm that satisfies the conditions in SOLPRU 1.1.2R or whose Part IV permission includes a requirement that it comply with the</u></p>

rules in SOLPRU.

*ultimate insurance
parent undertaking*

~~an insurance parent undertaking that is not itself the subsidiary
undertaking of another insurance parent undertaking.~~

Annex C

Amendments to the Senior Management Arrangements, Systems and Controls sourcebook (SYSC)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

1 Application and purpose

1.1A Application

- 1.1A.1 G The application of this sourcebook is summarised at a high level in the following table. The detailed application is set back in SYSC 1 Annex 1 and in the text of each chapter.

Type of firm	Applicable chapters
<i>Insurer (except for a UK Solvency II firm)</i>	Chapters 2, 3, 11 to 18, <u>20</u> , 21
<i>UK Solvency II firm</i>	<u>Chapters 3, 12, 18</u>
<i>Managing agent</i>	Chapters 2 , 3, 11 , 12, 18, 21
<i>Society</i>	Chapters 2 , 3, 12, 18, 21
Every other <i>firm</i>	Chapters 4 to 12, 18, 19A , 21

...

Annex 1 Detailed application of SYSC

Part 1	Application of SYSC 2 and SYSC 3 to an insurer, a managing agent and the Society		
	Who?		
1.1	R	<i>SYSC 2 and SYSC 3 only apply to an insurer, a managing agent and the Society (other than a managing agent, the Society, and a UK Solvency II firm) except that:</i>	
	(1)	for an incoming EEA firm or an incoming Treaty firm:	
		...	
	(1A)	<u>for an incoming EEA firm:</u>	

		(a)	<u>SYSC 2 does not apply;</u>
		(b)	<u>SYSC 3.1.1R to 3.1.5G, SYSC 3.2.1G to 3.2.5BG and SYSC 3.2.7G to 3.2.36R do not apply; and</u>
		(c)	<u>the remainder of SYSC 3 applies, but only in so far as responsibility for the matter in question is not reserved by an EU instrument to the firm's Home State regulator;</u>
...			
1.1A	R		<u>SYSC 2 and SYSC 3 do not apply to a UK Solvency II firm, except that SYSC 3.1.6R to 3.1.10G and SYSC 3.2.6R to 3.2.6KG do apply.</u>
1.1B	R		<u>SYSC 2 and SYSC 3 do not apply to the Society and managing agents, except that SYSC 3.1.6R to 3.1.10G and SYSC 3.2.6R to 3.2.6KG do apply to the Society and managing agents.</u>
...			
1.4	R		<u>SYSC 3.2.6AR to SYSC 3.2.6JG do not apply:</u>
		(1)	...
		(2)	in relation to the following <i>regulated activities</i> :
			...
		(c)	<i>long-term insurance business</i> which is outside the <i>Consolidated Life Directive Solvency II Directive</i> (unless it is otherwise one of the <i>regulated activities</i> specified in this rule);
			...
...			

2 Senior management arrangements

2.1 Apportionment of Responsibilities

...

2.1.4 R Allocation of functions

This table belongs to SYSC 2.1.3R

1: Firm type	2: Allocation of both functions must be to the following individual, if any (see Note):	3: Allocation to one or more individuals selected from this column is compulsory if there is no allocation to an
--------------	---	--

		individual in column 2, but is otherwise optional and additional:
(1) ...	...	...
(2) An <i>incoming EEA firm</i> or <i>incoming Treaty firm</i> (note: only the function in SYSC 2.1.3R(2) must be allocated) [deleted]	(not applicable)	the <i>firm's</i> and its <i>group's</i> : (1) <i>directors</i> ; and (2) <i>senior managers</i>
...		

...

2.1.6 G Frequently asked questions about allocation of functions in SYSC 2.1.3R

This table belongs to SYSC 2.1.5G

	Question	Answer
1	...	...
...		
12	How does the requirement to allocate the functions in SYSC 2.1.3R apply to an <i>incoming EEA firm</i> or <i>incoming Treaty firm</i> ?	<p>SYSC 1 Annex 1.1.1R and SYSC 1 Annex 1.1.8R restrict the application of SYSC 2.1.3R for such a <i>firm</i>. Accordingly:</p> <p>(1) Such such a firm is not required to allocate the function of dealing with apportionment in SYSC 2.1.3R(1).</p> <p>(2) Such a firm is required to allocate the function of oversight in SYSC 2.1.3R(2). However, the systems and controls that must be overseen are those relating to matters which the <i>FSA</i>, as <i>Host State regulator</i>, is entitled to regulate (there is <i>guidance</i> on this in SUP 13A Annex 2G). Those are primarily, but not exclusively, the systems and controls relating to the conduct of the <i>firm's</i> activities carried on from its <i>UK branch</i>.</p> <p>(3) Such a firm need not allocate the function of oversight to its <i>chief executive</i>; it must allocate it to one or more <i>directors</i> and <i>senior</i></p>

		<p>managers of the firm or the firm's group under SYSC 2.1.4R, row (2).</p> <p>(4) An incoming EEA firm which has provision only for cross border services is not required to allocate either function if it does not carry on regulated activities in the United Kingdom; for example if they fall within the overseas persons exclusions in article 72 of the Regulated Activities Order.</p> <p>See also Questions 1 and 15.</p>
...		

...

11 Liquidity risk systems and controls

11.1 Application

11.1.1 R SYSC 11 applies to an *insurer*, unless it is:

...

(5) an incoming *Treaty firm*; or

(6) a UK Solvency II firm.

...

12 Group risk systems and controls requirements

12.1 Application

...

12.1.2 R Except as set out in SYSC 12.1.4R, this section applies with respect to different types of *group* as follows:

- (1) SYSC 12.1.8R and SYSC 12.1.10R apply with respect to all *groups*, including *FSA regulated EEA financial conglomerates*, other *financial conglomerates* and *groups* dealt with in SYSC 12.1.13R to ~~SYSC 12.1.16R~~ SYSC 12.1.15R;
- (2) the additional requirements set out in SYSC 12.1.11R and SYSC 12.1.12R only apply with respect to *FSA regulated EEA financial conglomerates*; and
- (3) the additional requirements set out in SYSC 12.1.13R to SYSC ~~12.1.16R~~ SYSC 12.1.15R only apply with respect to *groups* of the

kind dealt with by whichever of those *rules* apply.

12.1.2A R This section applies with respect to different types of *insurer* and the *Society* as follows:

(1) only SYSC 12.1.1R to SYSC 12.1.5G, SYSC 12.1.11R and SYSC 12.1.12R apply to a *UK Solvency II firm* and the *Society*; and

(2) SYSC 12.1.11R and SYSC 12.1.12R do not apply to a *firm* that is not a *UK Solvency II firm* or the *Society*.

...

Purpose

...

12.1.7 G This section implements Articles 73(3) (Supervision on a consolidated basis of credit institutions) and 138 (Intra-group transactions with mixed activity holding companies) of the *Banking Consolidation Directive*, and Article 9 of the *Financial Groups Directive* (Internal control mechanisms and risk management processes) and Article 8 of the *Insurance Groups Directive* (Intra-group transactions).

...

Financial conglomerates

12.1.11 R Where this section applies with respect to a *financial conglomerate*, the risk management processes referred to in SYSC 12.1.8R(2) or, in the case of a *UK Solvency II firm* or the *Society*, the risk management system referred to in SOLPRU 9.3.1R(1) must include:

...

...

12.1.12 R Where this section applies with respect to a *financial conglomerate*, the internal control mechanisms referred to in SYSC 12.1.8R(2) or, in the case of a *UK Solvency II firm* or the *Society*, the internal control system referred to in SOLPRU 9.4.1R(1) must include:

...

Insurance undertakings

12.1.16 R ~~In the case of an *insurer* that has a *mixed-activity insurance holding company* as a *parent undertaking*, the risk management processes and internal control mechanisms referred to in SYSC 12.1.8R must include sound reporting and accounting procedures and other mechanisms that are adequate to identify, measure, monitor and control transactions between the *firm's parent undertaking mixed-activity insurance holding company* and~~

any of the ~~mixed-activity insurance holding company's subsidiary undertakings~~. [deleted]

- 12.1.17 G ~~SYSC 12.1.16R cannot apply to a building society as it cannot have a mixed-activity holding company as a parent undertaking. SYSC 12.1.16R cannot apply to a friendly society as it cannot have a mixed-activity insurance holding company as a parent undertaking.~~ [deleted]

...

13 Operational risk: systems and controls for insurers

13.1 Application

- 13.1.1 G SYSC 13 applies to an *insurer* unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

14 Prudential risk management and associated systems and controls for insurers

14.1 Application

- 14.1.1 R This section applies to an *insurer* unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

15 Credit risk management systems and controls for insurers

15.1 Application

- 15.1.1 G SYSC 15.1 applies to an *insurer* unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

16 Market risk management systems and controls for insurers

16.1 Application

16.1.1 G SYSC 16.1 applies to an *insurer* unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

17 Insurance risk systems and controls**17.1 Application**

17.1.1 G SYSC 17.1 applies to an *insurer* unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

20 Reverse stress testing**20.1 Application and purpose**

20.1 R (1) SYSC 20 applies to:

...

(b) an *insurer* unless it is:

...

(v) an *incoming Treaty firm*; or

(vi) a UK Solvency II firm.

...

20.2 Reverse stress testing requirements

...

20.2.2 R Where the *firm* is a member of:

(1) an *insurance group*, in respect of which it is required to maintain group capital; ~~[deleted]~~

...

it must conduct the reverse stress test on a solo basis as well as on a consolidated basis in relation to ~~the insurance group~~, the *UK consolidation group* or the *non-EEA sub-group*, as the case may be.

...

21 Risk control: additional guidance

21.1 Risk control: guidance on governance arrangements

21.1.1 G (1) This chapter provides additional guidance on risk-centric governance arrangements for effective risk management. It expands upon the general organisational requirements in *SYSC 2*, *SYSC 3*, *SYSC 4* and *SYSC 7*, and so applies to the same extent as *SYSC 3.1.1R* (for *insurers, managing agents and the Society*) and *SYSC 4.1.1R* (for every other *firm*).

...

(3) The *FSA* considers that *banks and insurers* that are included in the FTSE 100 Index are examples of the types of *firm* that should structure their risk control arrangements in this way. However, this *guidance* will also be relevant to some similar sized *firms* (whether or not *listed*) and some smaller *firms*, by virtue of their risk profile or complexity.

...

Annex D

Amendments to the Threshold Conditions (COND)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

2 The threshold conditions

2.1 Threshold condition 1: Legal status

...

- 2.1.2 G Section 40(1) of the *Act* (Application for permission) allows an application to be made to the *FSA* for *Part IV permission* by an individual, a *body corporate*, a *partnership* or an unincorporated association. However, in the case of the *regulated activities* of *accepting deposits* and *effecting or carrying out contracts of insurance*, the *Banking Consolidation Directive*, ~~the *First Non-Life Directive* and the *Consolidated Life Directive*~~ and the *Solvency II Directive* place further limits on the legal forms a *firm* may take. The *Act* implements the provisions of the directives and extends some of these limits to *firms* that are outside the scope of the directives.

...

2.4 Threshold condition 4: Adequate resources

...

- 2.4.2 G

...

- (3) High level systems and control requirements are in *SYSC* and in *SOLPRU* in relation to *UK Solvency II insurers*, the *Society* and *managing agents*. Detailed financial resources and systems requirements are in the relevant section of the Prudential Standards part of the *Handbook*, including specific provisions for particular types of *regulated activity*. The *FSA* will consider whether the *firm* is ready, willing and organised to comply with these requirements when assessing if it has adequate resources for the purposes of this *threshold condition*.

...

- 2.4.4 G (1) When assessing whether a *firm* will satisfy and continue to satisfy *threshold condition 4*, the *FSA* will have regard to all relevant matters, whether arising in the *United Kingdom* or elsewhere.

(2) Relevant matters may include but are not limited to:

...

(d) whether the *firm* has taken reasonable steps to identify and measure any risks of regulatory concern that it may encounter in conducting its business (see *COND 2.4.6G*) and has installed appropriate systems and controls and appointed appropriate human resources to measure them prudently at all times; see *SYSC 3.1* (Systems and Controls), *SYSC 3.2* (Areas covered by systems and controls), ~~and~~ *SYSC 4.1.1R* (Organisational requirements) and *SOLPRU 9* (Conditions governing business for *UK Solvency II firms*, the *Society* and *managing agents*); and

...

2.4.5 G In complying with *SYSC* (Systems and controls), a *firm* should plan its business appropriately so that it is able to identify, measure and manage the likely risks of regulatory concern it will face (*SYSC 3.2.17G* (Business strategy) and *SYSC 7* (Risk Control) and *SOLPRU 9* (Conditions governing business for *UK Solvency II firms*, the *Society* and *managing agents*)).

2.4.6 G ...

(3) The *FSA* would expect the level of detail in a *firm's* business plan or strategy plan in (2) to be appropriate to the complexity of the *firm's* proposed *regulated activities* and *unregulated activities* and the risks of regulatory concern it is likely to face (see *SYSC 3.2.11G* (Management information), ~~and~~ *SYSC 7* (Risk control) and *SOLPRU 9* (Conditions governing business for *UK Solvency II firms*, the *Society* and *managing agents*)). Notes on the contents of a business plan are given in the business plan section of the application pack for Part IV permission. A *firm* requiring specific *guidance* on the contents and level of detail of its business plan should contact the ~~Firm~~ Customer Contact Centre (020 7066 3954 0845 606 9966), or, if relevant, its usual supervisory contact at the *FSA*, or seek professional assistance.

...

2.5 Threshold condition 5: Suitability

...

2.5.2 G (1) *Threshold condition 5* (Suitability), requires the *firm* to satisfy the *FSA* that it is 'fit and proper' to have *Part IV permission* having regard to all the circumstances, including its connections with other *persons*, the range and nature of its proposed (or current) *regulated activities* and the overall need to be satisfied that its affairs are and

will be conducted soundly and prudently (see also *PRIN*, ~~and~~ *SYSC* and (for *UK Solvency II firms*, the *Society and managing agents*) *SOLPRU*).

...

...

- 2.5.6 G In determining whether a *firm* will satisfy, and continue to satisfy, threshold condition 5 in respect of conducting its business with integrity and in compliance with proper standards, the relevant matters, as referred to in *COND 2.5.4G(2)*, may include but are not limited to whether:

...

- (6) the *firm* has taken reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system that apply to the *firm* and the *regulated activities* for which it has, or will have, *permission* (see *SYSC 3.2.6R* to *SYSC 3.2.8R* (Compliance), ~~and~~ *SYSC 6.1.1R* to *SYSC 6.1.5R* and *SYSC 6.3*, and (for *UK Solvency II firms*, the *Society and managing agents*) *SOLPRU 9*);

...

...

2.6 Additional conditions

...

- 2.6.3 G This order implements requirements under the *Insurance Directives Solvency II Directive*, and the *Act* extends these requirements to *firms* outside of the *EEA*.

...

Annex E

Amendments to the Fit and Proper Test For Approved Persons (FIT)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

1 General

...

1.2 Introduction

...

1.2.4B **G** Under article 42 of the *Solvency II Directive*, the requirement to assess the fitness and propriety of persons who effectively run the *firm* or are responsible for other key *functions* is reserved to the *firm's Home State*. Therefore, the *FSA* will not assess the fitness and propriety of a *person* to perform a *controlled function* to the extent that the *controlled function* relates to the effective running of an *incoming EEA firm* that is a *Solvency II undertaking* or to responsibility for a key *function* of an *incoming EEA firm* that is a *Solvency II undertaking*. Where the *controlled function* relates to matters outside the scope of the *Solvency II Directive*, for example *money laundering* responsibilities (see CF11), the *FSA* will have regard to a *candidate's* competence and capability as well as his honesty, integrity, reputation and financial soundness.

...

Annex F

Amendments to the General Prudential sourcebook (GENPRU)

Note to reader: The Euro amounts in this Annex are based on the version of GENPRU as proposed to be amended in the Quarterly Consultation Paper No. 33 (CP 12/11) published on 6 June 2012 which is intended to come into force on 31 December 2012.

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

1 Application

1.1 Application

1.1.1 G There is no overall application statement for *GENPRU*. Each chapter or section has its own application statement.

1.1.2 G Broadly speaking however, *GENPRU* applies to:

(1) an *insurer* other than a UK Solvency II firm;

...

...

1.2 Adequacy of financial resources

Application

1.2.1 R This section applies to:

(1) a *BIPRU firm*; and

(2) an *insurer*, unless it is:

...

(e) an *incoming Treaty firm*; or

(f) a UK Solvency II firm.

...

...

1.2.10 G ~~The scope of application of this section is not restricted to *insurers* that are subject to the relevant *EU Directives*. [deleted]~~

...

Application of this section on a solo and consolidated basis: Processes and tests

- 1.2.45 R ~~If an *insurer* is a member of an *insurance group* and *INSPRU* 6.1.9R, *INSPRU* 6.1.10R or *INSPRU* 6.1.15R (Requirement to maintain group capital) apply to it with respect to that *insurance group* the *ICAAP rules*:~~
- ~~(1) apply to that *insurer* on a consolidated basis; and~~
 - ~~(2) do not apply to it on a solo basis. [deleted]~~
- ...
- 1.2.47 R The *ICAAP rules* apply on a solo basis:
- (1) to an *insurer* ~~to which those *rules* do not apply on a consolidated basis under *GENPRU* 1.2.45R;~~
- ...
- 1.2.48 R The requirements of the *ICAAP rules* as they apply on a consolidated basis must be carried out on the basis of the consolidated position of:
- (1) ~~(if *GENPRU* 1.2.45R applies) that *insurance group*; [deleted]~~
- ...
- 1.2.49 R (1) In accordance with the general principles in *GENPRU* 1.2.48R and *BIPRU* 8 (Group risk - consolidation), for the purpose of the *ICAAP rules* as they apply on a consolidated basis:
- ...
- (e) references to the *CRR* are to the consolidated capital requirements applicable to the relevant group under *BIPRU* 8 (Group risk - consolidation) ~~or, as the case may be, *INSPRU* 6 (Group risk: Insurance groups);~~
- ...
- (2) For the purpose of this *rule* the relevant group is the group referred to in *GENPRU* 1.2.48R and the members of that group are those *undertakings* that are included in the scope of consolidation with respect to the ~~*insurance group*~~, *UK consolidation group* or, as the case may be, *non-EEA sub-group* in question.
- ...
- ...
- 1.2.55 G The purpose of *GENPRU* 1.2.51R – *GENPRU* 1.2.53R is to enable the *FSA* to assess the extent, if any, to which a *firm's* assessment, calculated on a consolidated basis, is lower than it would be if each separate legal entity

were to assess the amount of capital it would require to mitigate its risks (to the same level of confidence) were it not part of a group subject to consolidated supervision under *BIPRU* 8 (Group risk – consolidation) ~~or *INSURU* 6.1 (Group risk: Insurance groups)~~. ...

...

Group risk (BIPRU firm only)

...

1.2.88 G A *firm* should include in the written record referred to in *GENPRU* 1.2.60R a description of the broad business strategy of ~~the *insurance group*~~, the *UK consolidation group* or the *non-EEA sub-group* of which it is a member, the group's view of its principal risks and its approach to measuring, managing and controlling the risks. This description should include the role of stress testing, scenario analysis and contingency planning in managing risk at the solo and consolidated level.

1.2.89 G A *firm* should satisfy itself that the systems (including IT) of ~~the *insurance group*~~, the *UK consolidation group* or the *non-EEA sub-group* of which it is a member are sufficiently sound to support the effective management and, where applicable, the quantification of the risks that could affect ~~the *insurance group*~~, the *UK consolidation group* or the *non-EEA sub-group*, as the case may be.

...

1.3 Valuation

Application

1.3.1 R (1) This section of the *Handbook* applies to an *insurer*, unless it is:

...

(b) an *incoming EEA firm*; ~~or~~

(c) an *incoming Treaty firm*; or

(d) a *UK Solvency II firm*.

...

General requirements: Accounting principles to be applied

...

1.3.8 G ~~Articles 23.3(viii) and 24.2(iv) of the *Consolidated Life Directive* require assets of an *insurer* that are managed on its behalf by a *subsidiary undertaking* to be taken into account for the purposes of determining the *insurer's admissible assets* and its assets in excess of concentration limits.~~

The application of *GENPRU* 1.3.4R will result in ~~such assets remaining the~~ assets of an insurer that are managed on its behalf by a subsidiary undertaking remaining on the balance sheet of the insurer.

...

Shares in and debts due from related undertakings

...

1.3.46 R In relation to *shares* in, and debts due from, an *undertaking* referred to in *GENPRU* 1.3.43R(1), *GENPRU* 1.3.45R does not apply for the purposes of *GENPRU* 2.2.256R (Adjustments for regulated related undertakings other than insurance undertakings) ~~and *INSPRU* 6.1 (Group risk: Insurance groups)~~.

1.3.47 R For the purposes of *GENPRU* 1.3.45R, the value of the *shares* held in an *undertaking* referred to in *GENPRU* 1.3.43R(1) or *GENPRU* 1.3.43R(3) is the sum of:

...

(3) for other purposes in *GENPRU* and *INSPRU*, the sum of:

...

(b) if the *undertaking* is an *insurance undertaking*, its ineligible surplus capital and any restricted assets of the *undertaking* ~~which have been excluded under *INSPRU* 6.1.41R(1)~~.

1.3.47A R For the purposes of *GENPRU* 1.3.47R(3)(b), the ineligible surplus capital of the *undertaking* is calculated by deducting B from A where:

(1) A is the *regulatory surplus value* of that *undertaking* less any restricted assets it may hold; and

(2) B is the transferable capital of that *undertaking*.

1.3.47B R For the purposes of *GENPRU* 1.3.47R(3)(b) and *GENPRU* 1.3.47AR(1), “restricted assets” means assets of the *undertaking* which are subject to a legal restriction or other requirement having the effect that those assets cannot be transferred or otherwise made available to the *firm* for the purposes of the *firm* meeting its *capital resources requirement* calculated in accordance with *GENPRU* 2.1 without causing a breach of that legal restriction or requirement.

...

1.3.51 R For the purposes of *GENPRU* 1.3.47R to *GENPRU* 1.3.50R:

(1) ...

(a) subject to (2), *individual capital resources requirement* has

the meaning given by ~~INSPRU 6.1.34R~~ GENPRU 1.3.51AR;

(b) total capital after deductions means:

...

(c) ineligible surplus capital has the meaning given by ~~INSPRU 6.1.67R~~ GENPRU 1.3.47AR;

...

1.3.51A R For the purposes of GENPRU 1.3.51R(1)(a) an *individual capital resources requirement* is:

- (1) in respect of a *UK Solvency II firm*, the *SCR*;
- (2) in respect of an *EEA insurer* or an *EEA pure reinsurer* that is a *Solvency II undertaking*, the equivalent of the *SCR* as calculated in accordance with the *Solvency II EEA implementing measures* in its *Home State*;
- (3) in respect of a *third country insurance undertaking* or *third country reinsurance* undertaking to which *SOLPRU 11.4.18R(2)* applies, the equivalent of the *SCR* as calculated in accordance with the applicable requirements in that third country;
- (4) in respect of any *UK insurer* other than a *UK Solvency II firm*, its *capital resources requirement* calculated in accordance with *GENPRU 2.1*;
- (5) in respect of an *EEA insurer* or an *EEA pure reinsurer* that is not a *Solvency II undertaking*, the equivalent of the *capital resources requirement* as calculated in accordance with the applicable requirements in its *Home State*;
- (6) in respect of an *EEA ISPV*, the solo capital resources requirement that applies to the *ISPV* under the *sectoral rules* for the *insurance sector* of the member State of the *competent authority* that authorised the *ISPV*;
- (7) in respect of an *insurance undertaking* that is not within (1) to (5), and whose head office is in a *designated State or territory*, either:
 - (a) its *proxy capital resources requirement*; or
 - (b) the solo capital resources requirement that applies to it under the *sectoral rules* for the *insurance sector* of the *designated State or territory*;
- (8) in respect of an *insurance undertaking* within (7) which is not subject to a solo capital resources requirement under the *sectoral rules* for the *insurance sector* of the *designated State or territory*, its

proxy capital resources requirement;

- (9) in respect of an insurance undertaking that is not within (1) to (8), its proxy capital resources requirement;
- (10) in respect of an insurance holding company, zero;
- (11) in respect of a regulated entity (excluding an insurance undertaking), its solo capital resources requirement;
- (12) in respect of an asset management company, the solo capital resources requirement that would apply to it if, in connection with its activities, it were treated as being in the investment services sector; and
- (13) in respect of a financial institution that is not a regulated entity (including a financial holding company), the solo capital resources requirement that would apply to it if, in connection with its activities, it were treated as being within the banking sector.

1.3.52 G GENPRU 1.3.47R to GENPRU 1.3.51R set out several different valuation bases for an insurer's shares in related undertakings. The regulatory surplus value (defined in GENPRU 1.3.48R) measures the related undertaking's own capital surplus or deficit. This is used: ~~(i) in GENPRU 1.3.47R as a basis for calculating the impact on the firm's firm's position of its investments in related undertakings; and (ii) in INSPRU 6.1 as a starting point for the calculation of ineligible surplus capital.~~

...

1.3.54 G ~~The rules that specify how, for the purposes of the adjusted solo capital calculation, an insurer should incorporate its related undertakings into its capital resources and capital resources requirement are set out in INSPRU 6.1. [deleted]~~

...

~~General insurance business: Community co-insurance operations—~~

1.3.57 R ~~Where a relevant insurer determines the amount of a liability in order to make provision for outstanding claims under a Community co-insurance operation, then, if the leading insurer has informed the relevant insurer of the amount of the provision made by the leading insurer for such claims, the amount determined by the relevant insurer:~~

- ~~(1) must be at least as great as the amount of the provision made by the leading insurer; or~~
- ~~(2) in a case where it is not the practice in the United Kingdom to make such provision separately, must be sufficient, when all liabilities are taken into account, to include provision at least as great as that made~~

by the *leading insurer* for such *claims*,

due regard being had in either case to the proportion of the risk covered by the *relevant insurer* and by the *leading insurer* respectively. [deleted]

...

GENPRU 1.5 is deleted in its entirety. The deleted text is not shown.

...

2 Capital

2.1 Calculation of capital resources requirements

Application

2.1.1 R This section applies to:

...

(2) an *insurer*, unless it is:

...

(e) an *incoming Treaty firm*; or

(f) a *UK Solvency II firm*.

2.1.2 G The scope of application of this section is not restricted to *firms* that are subject to the relevant *EU Directives*. [deleted]

...

2.1.8 G (1) This section implements minimum EC standards for the *capital resources* required to be held by an *insurer* undertaking business that falls within the scope of the *Consolidated Life Directive* (2002/83/EC), the *Reinsurance Directive* (2005/68/EC) or the *First Non-Life Directive* (1973/239/EEC) as amended. [deleted]

...

Main requirement: Insurers

2.1.13 R (1) Subject to (2), an An *insurer* must maintain at all times *capital resources* equal to or in excess of its *capital resources requirement* (*CRR*).

(2) ~~An *insurer* which is a *participating insurance undertaking* and, in relation to its own *group capital resources*, is in compliance with *INSPRU 6.1.9R* (Requirement to maintain group capital), is deemed to comply with this *rule*.~~ [deleted]

...

Calculation of the MCR (Insurer only)

...

- 2.1.27 G ~~The MCR gives effect to the EU Directive minimum requirements. For general insurance business, the EU Directive minimum is the higher of the general insurance capital requirement and the relevant base capital resources requirement. For long term insurance business, the EU Directive minimum is the higher of the long term insurance capital requirement and the base capital resources requirement. For pure reinsurers and captive reinsurers carrying on both general insurance business and long term insurance business, however, the base capital resources requirement is the EU Directive required minimum only when it is higher than the sum of the general insurance capital requirement and the long term insurance capital requirement. The base capital resources requirement is the minimum guarantee fund for the purposes of article 29(2) of the Consolidated Life Directive (2002/83/EC), article 17(2) of the First Non-Life Directive (1973/239/EEC) as amended and article 40(2) of the Reinsurance Directive (2005/68/EC). The resilience capital requirement is an FSA minimum requirement for long term insurance business for regulatory basis only life firms that is additional to the EU minimum requirement for long term insurance business. [deleted]~~

...

Table: Base capital resources requirement for an insurer

- 2.1.30 R This table belongs to GENPRU 2.1.29R

Firm category		Amount: Currency equivalent of
General insurance business		
Liability insurer (classes 10-15)	Directive A mutual that is a Solvency I firm	€2.775 million £2.425 million
	Non-directive An insurer that is a non-Solvency I firm	€350,000 £306,000
	Other (including mixed insurer but excluding pure reinsurer) [Note: this category currently includes a placemaker for any new firms that are not Solvency II firms, whether they would have fallen within the scope of the	€3.7 million £3.23 million

	<u>Solvency I Directive or outside the scope of Solvency I if Solvency I was still in force]</u>	
Other insurer	<u>Directive A mutual that is a Solvency I firm</u>	€1.875 million £1.64 million
	<u>Non-directive An insurer that is a non-Solvency I firm (classes 1 to 8, 16 or 18)</u>	€260,000 £227,000
	<u>Non-directive An insurer that is a non-Solvency I firm (classes 9 or 17)</u>	€175,000 £153,000
	Mixed insurer	€3.7 million £3.23 million
	Other (excluding pure reinsurer) [Note: this category currently includes a placemaker for any new firms that are not Solvency II firms, whether they would have fallen within the scope of the Solvency I Directive or outside the scope of Solvency I if Solvency I was still in force]	€2.5 million £2.185 million
Long-term insurance business		
Mutual	<u>Directive A mutual that is a Solvency I firm</u>	€2.775 million £2.425 million
	<u>Non-directive A mutual that is a non-Solvency I firm</u>	€700,000 £611,000
	[Placemaker for any new firms that are not Solvency II firms, whether they would have fallen within the scope of the Solvency I Directive or outside the scope of Solvency I if Solvency I was still in force]	[]
	Any other insurer (including mixed insurer but excluding pure reinsurer)	€3.7 million £3.23 million
All business (general insurance business and long-term insurance business)		

<i>Pure reinsurer excluding captive reinsurer</i>	€3.7 million <u>£3.23 million</u>
<i>Captive reinsurer</i>	€1.2 million <u>£1.05 million</u>

- 2.1.31 G (1) Under the *Insurance Directives* the amount of the *base capital resources requirement* specified in the last column of the table in *GENPRU 2.1.30R* for an *insurer* which is not a *Non-directive insurer* is subject to annual review. The relevant amounts will be increased by the percentage change in the European index of consumer prices (comprising all EU member states, as published by Eurostat) from 20 March 2002, to the relevant review date, rounded up to a multiple of €100,000, provided that where the percentage change since the last increase is less than 5%, no increase will take place. [deleted]
- (2) Similar provisions for the index-linking of the *base capital resources requirement* are included in the *Reinsurance Directive*, although in that case the index-linking starts from 10 December 2005. However, to ensure consistency as between all *firms* affected by the index-linking of the *base capital resources requirement* under the *Insurance Directives* and the *Reinsurance Directive*, the *FSA* intends, so far as possible, to amend the amounts in *GENPRU 2.1.30R* for all such *firms* (and *GENPRU 2.3.9R* for the *base capital resources requirements* applying to Lloyd's) when an index-linked increase is required by the *Insurance Directives*. The *FSA* may, however, have to depart from this approach where the result would be that the *base capital resources requirement* required for any type of *firm* under *GENPRU 2.1.30R* is less than the increased amount resulting from the operation of an index-linking provision to which it is subject. [deleted]
- 2.1.32 G Any increases in the *base capital resources requirement* referred to in *GENPRU 2.1.31 G* will be published on the *FSA* website. [deleted]
- 2.1.33 R In the case of an *insurer* and for the purposes of the *base capital resources requirement*, the exchange rate from the Euro to the pound sterling for each year beginning on 31 December is the rate applicable on the last day of the preceding October for which the exchange rates for the currencies of all the European Union member states were published in the Official Journal of the European Union. [deleted]

...

2.2 Capital resources

Application

- 2.2.1 R This section applies to:
- ...
- (2) an *insurer* unless it is:
- ...
- (e) an *incoming Treaty firm*; or
- (f) a UK Solvency II firm.

Purpose

- ...
- 2.2.3 G This section implements minimum EC standards for the composition of *capital resources* required to be held by an *insurer* undertaking business that falls within the scope of the *Consolidated Life Directive* (2002/83/EC), the *First Non-Life Directive* (1973/239/EEC) as amended or the *Reinsurance Directive* (2005/68/EC). [deleted]
- 2.2.4 G This section ~~also~~ implements minimum EC standards for the composition of *capital resources* required to be held by a *BIPRU firm*. In particular it implements Articles 56 - 61, Articles 63 - 64, Article 66 and Articles 120 - 122 of the *Banking Consolidation Directive* (2006/48/EC) and Articles 12 - 16, Article 17 (in part), Article 22(1)(c) (in part) and paragraphs 13 - 15 of Part B of Annex VII of the *Capital Adequacy Directive* (2006/49/EC).

...

Calculation of capital resources: Insurers

- 2.2.22 G *Capital resources* for an *insurer* can be calculated either as the total of eligible assets less foreseeable liabilities (~~which is the approach taken in the *Insurance Directives*~~) or by identifying the components of capital. ...

...

Limits on the use of different forms of capital: Insurers

- ...
- 2.2.36 G The purpose of the requirements in ~~GENPRU 2.2.33R to GENPRU 2.2.34AR~~ is to comply with the requirements of the *Insurance Directives* and the *Reinsurance Directive* that an insurer must maintain a *guarantee fund* of higher quality *capital resources* items. [deleted]

...

- 2.2.40 G ~~GENPRU 2.2.32R, GENPRU 2.2.37R and GENPRU 2.2.38R give effect to the requirements of the *Insurance Directives* and the *Reinsurance Directive* that no more than 50% of the amount which is the lesser of the available solvency margin and the required solvency margin should consist of *tier two capital resources* and that no more than 25% of that amount should consist of *lower tier two capital resources*. [deleted]~~

...

Notification of issuance of capital instruments

...

- 2.2.61H G Details of the notification to be provided by a *BIPRU firm* in relation to *capital instruments* issued by another *undertaking* in its *group* for inclusion in its *capital resources* or the *consolidated capital resources* of its *UK consolidation group* or *non-EEA sub-group* are set out in *BIPRU 8.6.1AR* to *BIPRU 8.6.1FR*. ~~Details of the notification to be provided by an *insurer* in relation to *capital instruments* issued by another *undertaking* in its *group* for inclusion in its *group capital resources* are set out in *INSPRU 6.1.43AR* to *INSPRU 6.1.43FR*.~~

...

Deductions from tiers one and two: Material holdings (BIPRU firm only)

...

- 2.2.213 R An item falls into this provision for the purpose of *GENPRU 2.2.212R* if it is:

...

- (2) ~~subordinated debt or another item of capital that falls into Article 16(3) of the *First Non-Life Directive* or, as applicable, Article 27(3) of the *Consolidated Life Directive* is an item of basic own funds under *SOLPRU 3*.~~

...

Deductions from total capital: Adjustments for related undertakings

...

- 2.2.258 G ~~*Related undertakings* which are also *insurance undertakings* are not included in *GENPRU 2.2.256R* because an *insurer* that is a *participating insurance undertaking* is subject to the requirements of *INSPRU 6.1 (Group Risk: Insurance Groups)*. [deleted]~~

Deductions from total capital: Illiquid assets (BIPRU investment firm only)

...

2.2.268 G Subject to a *waiver*, ~~under the *Insurance Directives*~~ a maximum of one half of unpaid *share* capital or, in the case of a *mutual*, one half of the *unpaid initial fund* may be included in an *insurer's capital resources*, once the paid-up part amounts to 25% of that *share* capital or fund, up to 50% of total *capital resources*.

2.2.269 G In the case of a *mutual* carrying on *general insurance business* and subject to a *waiver*, calls for supplementary contributions within the *financial year* may only be included in a *firm's capital resources* up to a maximum of 50% of the difference between the maximum contributions and the contributions actually called in, subject to a limit of 50% of total *capital resources*. In the case of a *mutual* carrying on *long-term insurance business*, ~~the *Consolidated Life Directive* does not permit~~ calls for supplementary contributions ~~to~~ cannot be included in a *firm's capital resources*.

Other requirements: insurers carrying on with-profits business (Insurer only)

2.2.270 R *GENPRU 2.2.270R to GENPRU 2.2.275G* only apply to an *insurer* falling within *GENPRU 2.2*.

...

2.2.275 G ...

(2) For *firms* which are *realistic basis life firms* compliance with *GENPRU 2.2.271R(3)* would usually be achieved if the *capital instrument* provides that no amounts will be payable under it unless the *firm's capital resources* exceed its *capital resources requirement*. However, such *firms* should ensure that the terms of the *capital instrument* refer to *FSA capital resources requirements* in force from time to time, including the current realistic reserving requirements ~~and are not restricted to former minimum capital requirements based only on the *Insurance Directives'* required minimum margin of solvency~~. For *firms* which are not *realistic basis life firms*, compliance with *GENPRU 2.2.271R(3)* will probably require specific reference to be made to treating *customers* fairly in the terms of the *capital instrument*.

GENPRU 2.3 is deleted in its entirety. The deleted text is not shown.

...

2 Annex 1 Capital resources table for an insurer

R

Capital resources calculation for an insurers		
Type of capital	Related text	Stage
...		

<i>Implicit items</i> [deleted]	GENPRU 2 Annex 8G	
...		

...

GENPRU 2 Annex 8G is deleted in its entirety. The deleted text is not shown.

...

3 Cross sector groups

3.1 Application

R (1) *GENPRU 3.1* applies to every *firm* that is a member of a *financial conglomerate* other than

...

(c) a *UCITS* qualifier; ~~and~~

(d) an *ICVC*; ~~and~~

(e) an insurer that is not a *UK Solvency II* firm.

...

Capital adequacy requirements: introduction

...

3.1.18 G Part 4 of *GENPRU 3 Annex 1R* (Use of Method 4 from Annex I of the *Financial Groups Directive*) applies the *FSA's sectoral rules* with respect to the *financial conglomerate* as a whole, with some adjustments. Where Part 4 of *GENPRU 3 Annex 1R* applies the *FSA's sectoral rules* for:

(1) the *insurance sector*, that involves ~~a combination of Methods 2 and 3~~ Method 1 (unless the *FSA* has required the application of Method 2, or a combination of Methods 1 and 2); and

...

...

Risk concentration and intra-group transactions: Table of applicable sectoral rules

3.1.36 R Table: application of sectoral rules
This table belongs to *GENPRU 3.1.35R*

The most important financial sector	Applicable sectoral rules
-------------------------------------	---------------------------

	Risk concentration	Intra-group transactions
...		
<i>Insurance sector</i>	None <u>SOLPRU 11.8.1R</u>	Rule 9.39 of IPRU(INS) <u>SOLPRU 11.8.2R</u>
...		

...

3.2 Third-country groups

Application

3.2.1 R *GENPRU 3.2* applies to every *firm* that is a member of a *third-country group*. But it does not apply to:

...

(4) an *ICVC*; or

(5) an insurer that is not a UK Solvency II firm.

...

3.2.4 G If the supervision of a *third-country group* by a *third-country competent authority* does not meet the equivalence test referred to in *GENPRU 3.2.3G*, *competent authorities* may apply other methods that ensure appropriate supervision of the *EEA regulated entities* in that *third-country group* in accordance with the aims of supplementary supervision under the *Financial Groups Directive* or consolidated supervision (including, in the case of the insurance sector, group supervision) under the applicable *EEA prudential sectoral legislation*, to the *EEA regulated entities* in the *banking sector*, *investment services sector* and (in the case of a *financial conglomerate*) *insurance sector*.

...

3 Annex 1 Capital adequacy calculations for financial conglomerates (GENPRU 3.1.26R and GENPRU 3.1.29R)

R ...
5 Table: Paragraph 4.2: Application of sectoral consolidation rules

Type of financial conglomerate	Applicable sectoral consolidation rules
<i>Banking and investment services conglomerate</i>	<i>BIPRU 8</i> and <i>BIPRU TP</i> , subject to paragraph 4.5.
<i>Insurance conglomerate</i>	<i>INSPRU 6.1</i> <u><i>SOLPRU 11</i></u> amended

	in accordance with Part 5.
--	----------------------------

7 Table

A mixed financial holding company	4.4	A <i>mixed financial holding company</i> must be treated in the same way as: (1) a <i>financial holding company</i> (if the <i>rules</i> in <i>BIPRU</i> 8 are applied); or (2) an <i>insurance holding company</i> (if the <i>rules</i> in <i>INSPRU</i> <i>6.4 SOLPRU</i> 11 are applied).
-----------------------------------	-----	---

8 Table: PART 5: Principles applicable to all methods

...		
Application of sectoral rules: General	5.4	The following adjustments apply to the <i>applicable sectoral rules</i> as they are applied by the <i>rules</i> in this annex. (1) ... (2) If any of those <i>rules</i> would otherwise not apply to a situation in which they are applied by <i>GENPRU</i> 3 Annex 1R, those <i>rules</i> nevertheless still apply (and in particular, any of those <i>rules</i> that would otherwise have the effect of disapplying consolidated supervision (or, in the case of the insurance sector, supplementary supervision) do not apply). (3) ...
Application of sectoral rules: Insurance sector	5.5	(1) This <i>rule</i> applies an adjustment to the <i>applicable sectoral rules</i> for the <i>insurance sector</i> as they are applied by the <i>rules</i> in this annex. (2) To the extent that: (a) those <i>rules</i> merely require a report on whether or not a specified level of solvency is met (a soft limit); or (b) the requirements in those <i>rules</i> concern having certain net assets of an amount at or above certain levels; • those requirements are restated so as to include an obligation at all times actually to have capital at or above that level (a hard limit), thereby turning a soft limit into a hard limit and turning a limit drafted by reference

		to assets and liabilities into a requirement that the level of capital be maintained at or above a specified level. If those <i>rules</i> apply both a hard and a soft limit, and the level of the soft limit is higher, that soft limit is applied under this annex, but translated into a hard limit in accordance with the earlier provisions of this <i>rule</i> . [deleted]
No capital ties	5.7 ...	<p>(4) If:</p> <p>(a) <i>GENPRU</i> 3.1.26R applies with respect to a <i>financial conglomerate</i> falling into (1) under <i>GENPRU</i> 3.1.27R(2) (Use of <i>Part IV permission</i> to apply Annex I of the <i>Financial Groups Directive</i>); or</p> <p>(b) <i>GENPRU</i> 3.1.29R (Capital adequacy requirements: Application of Methods 1, 2 or 3 from Annex I of the <i>Financial Groups Directive</i>) applies with respect to a <i>financial conglomerate</i> falling into (1);</p> <p>then:</p> <p>(c) the treatment of the links in (1) (including the treatment of any <i>solvency deficit</i>) is as provided for in the <i>requirement</i> referred to in <i>GENPRU</i> 3.1.30R; and</p> <p>(d) <i>GENPRU</i> 3.1.26R or <i>GENPRU</i> 3.1.29R, as the case may be, apply even if the <i>applicable sectoral rules</i> do not deal with how <i>undertakings</i> not linked by capital ties are to be dealt with for the purposes of consolidated supervision (or, in the case of the <i>insurance sector</i>, supplementary supervision).</p> <p>...</p>

9 Table: PART 6: Definitions used in this Annex

...		
Solo capital resources requirement: Insurance sector	6.4	<p>(1) The <i>solo capital resources requirement</i> of an <i>undertaking</i> in the <i>insurance sector</i> must be calculated in accordance with this <i>rule</i>.</p> <p>(2) Subject to (3), the <i>solo capital resources requirement</i> of an <i>undertaking</i> in the <i>insurance sector</i> is the <i>capital</i></p>

	<p>resources requirement <i>individual capital resources requirement</i> identified in <i>INSPRU 6.1.34R(1) to (8)</i> <i>GENPRU 1.3.51AR</i> as applying to that <i>undertaking</i>. (3) INSPRU 6.1.34R(1)(b) does not apply for the purposes of this annex.</p>
...	

...

11 Table: Paragraph 6.10: Application of sectoral consolidation rules

Financial sector	FSA's sectoral rules
...	
<i>Insurance sector</i>	INSPRU 6.1. <i>SOLPRU 11</i>
...	

...

3 Annex 3 Guidance Notes for Classification of Groups

G This annex consists only of one or more forms. Forms are to be found through the following address:

Classification of Groups (GENPRU 3.1.3 G) - FSA/docs/genpru/genpru_ch3_annex3G.pdf

...

General guidance

We would like this to be completed based on the most senior parent in the group, and, if applicable, for the company heading the most senior conglomerate group in the EEA. If appropriate, please also attach a list of all other likely conglomerate sub-groups.

Please use the most recent accounts for the top level company in the group together with the corresponding accounts for all subsidiaries and participations that are included in the consolidated accounts. Please indicate the names of any significant subsidiaries with a different year-end from the group's year-end.

Please note the following:

- (a) Branches should be included as part of the parent entity.
- (b) Include in the calculations overseas entities owned by the relevant group or sub-group.
- (c) There are only two sectors for this purpose: banking/investment and insurance.
- (d) You will need to assign non-regulated financial entities to one of these sectors:
 - **banking/investment** activities are listed in - Annex 1 to the Banking Consolidation Directive
 - **insurance** activities are listed in ~~IPRU Insurers Annex 11.1 and 11.2~~ p

~~163–168.~~ schedule 1 to the *Regulated Activities Order*.

• Any operator of a UCITS scheme, insurance intermediary, mortgage broker and mixed financial holding company does not fall into the directive definitions of either financial sector or insurance sector and should be treated for these purposes as being outside the financial sector. They should therefore be ignored for the purposes of these calculations.

...

...

TP 1 Application of GENPRU TP 1 to GENPRU TP 6 and other general provisions for insurers

Application of GENPRU TP 1 to GENPRU TP 6

- 1.1 R *GENPRU TP 1 - GENPRU TP 6 apply to an insurer, other than a UK Solvency II firm.*
- 1.2 G *GENPRU TP 1 - GENPRU TP 6 apply to an insurer to whom the relevant GENPRU rule listed in GENPRU TP Table 3R, GENPRU TP 4.3R, GENPRU TP 5.2R or GENPRU TP 6.2R applies. An insurer to whom GENPRU does not apply (including a UK Solvency II firm) is not subject to GENPRU TP.*

...

TP 4 Capital instruments

...

Waivers

- 4.3 R Subject to *GENPRU TP 4.4R* and to compliance with the conditions set out in *GENPRU TP 4.6R*, a *firm* will be treated as complying with *GENPRU 2.2.271R(3)*, *GENPRU 2.2.177R(2)*, *GENPRU 2.2.177R(3)*, *GENPRU 2.2.180R* and *GENPRU 2.2.181R*, in relation to the capital instrument to which the *waiver* or written concession referred to in *GENPRU TP 4.2R* related, so long as the *firm* is not obliged to pay any interest under the terms of the capital instrument in circumstances where the *firm* does not have *capital resources* equal to or in excess of its ~~required~~ margin of solvency as required under the *Insurance Directives* immediately before the *Solvency II implementation date*.

...

TP 5 Calls for supplementary contributions

...

Application

5.2 R GENPRU TP 5 applies to a *firm*, other than a UK Solvency II firm, the Society and managing agents which immediately before 31 December 2004 had the benefit of a *waiver* in relation to *IPRU(INS)* rule 2.10(4).

...

Annex G

Amendments to the Prudential sourcebook for Banks, Building Societies and Investment Firms (BIPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

5.5 Other funded credit risk mitigation

...

Life insurance policies: Minimum requirements

5.5.5 R For life insurance policies pledged to a *lending firm* to be recognised the following conditions must be met:

- (1) the party providing the life insurance must be subject to ~~Directive 2002/83/EC and Directive 2001/17/EC of the European Parliament and of the Council~~ the Solvency II Directive, or is subject to supervision by a competent authority of a third country which applies supervisory and regulatory arrangements at least equivalent to those applied in the Community;

...

TP 3 Pre CRD capital requirements applying on a solo basis during 2007

...

Disapplication of *GENPRU* and *BIPRU*

3.8 R ...

GENPRU and BIPRU provisions	...
...	...
GENPRU 1.5 (Application of GENPRU 1 to Lloyd's) [deleted]	Not applicable as does not apply to <i>BIPRU firms</i> [deleted]
...	...
GENPRU 2.3 (Application of GENPRU 2 to Lloyd's) [deleted]	Not applicable as does not apply to <i>BIPRU firms</i> [deleted]

...

TP 15 Commodities firm transitionals: Exemption from capital requirements

...

15.10 G ...

GENPRU and BIPRU provisions	...
...	...
GENPRU 1.5 (Application of GENPRU 1 to Lloyd's) [deleted]	Not applicable as does not apply to BIPRU firms [deleted]
...	...
GENPRU 2.3 (Application of GENPRU 2 to Lloyd's) [deleted]	Not applicable as does not apply to BIPRU firms [deleted]

...

Annex H

Amendments to the Prudential sourcebook for Insurers (INSPRU)

Note to reader: The Euro amounts in this Annex are based on the version of INSPRU as proposed to be amended in the Quarterly Consultation Paper No. 33 (CP 12/11) published on 6 June 2012 which is intended to come into force on 31 December 2012.

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise indicated.

1 Capital resources requirements and technical provisions for insurance business

1.1 Application

1.1.1 R *INSPRU* 1.1 applies to an *insurer* unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

1.1.6 G This section may apply in cases where a *firm* has its head office in another *EEA State* but is neither an *incoming EEA firm* nor an *incoming Treaty firm*; ~~this could arise in the case of a non-directive mutual.~~

Purpose

...

1.1.9 G ~~This section implements requirements of the *Insurance Directives* for both *general insurance business* and *long-term insurance business* with regard to the *technical provisions*. The relevant articles of the Directives include:~~

(1) ~~article 15 of the *First Non-Life Directive*, as substituted by article 17 of the *Third Non-Life Directive*; and~~

(2) ~~article 20 of the *Consolidated Life Directive* (this Directive consolidates the provisions of the previous *First, Second* and *Third Life Directives*. [deleted]~~

...

Establishing technical provisions

- 1.1.12 R For *general insurance business*, a *firm* must establish adequate technical provisions:
- (1) ~~in accordance with the rules in INSPRU 1.4 for *equalisation provisions*; and~~
- (2) ~~otherwise~~, in accordance with *GENPRU* 1.3.4R.
- 1.1.13G G For *general insurance business*, the *technical provisions* include outstanding *claims* provisions, *unearned premiums* provisions, and unexpired risk provisions ~~and *equalisation provisions*~~. These provisions take into account the expected ultimate cost of *claims*, including those not yet incurred, and related expenses ~~and include an allowance for smoothing *claims* (the *equalisation provision*)~~.
- ...
- 1.1.15 G ~~For some categories of *general insurance business*, *equalisation provisions* are required. These ensure that a *firm* retains additional assets to provide some extra protection against uncertainty as to the amount of *claims*. *Equalisation provisions* are particularly suitable for volatile business, where *claims* in any future year may be subject to significant adverse deviation from recent or average expected *claims* experience, or where trends in *claims* experience may be subject to change. Such volatile *claims* experience arises in a number of types of business, for example, property, marine and aviation, nuclear, certain *non-proportional reinsurance treaty* business, and credit insurance. The *equalisation provisions* help to equalise fluctuations in loss ratios in future years (see *INSPRU* 1.4 (*Equalisation provisions*)).~~
[deleted]
- ...
- 1.1.34A G *INSPRU* 1.1.34R is not applied to *pure reinsurers* because they are subject under *INSPRU* 3.1.61AR to the "prudent person" investment principles ~~from the *Reinsurance Directive*~~.
- ...
- Capital requirements for insurers
- 1.1.43 G ...
- (2) ~~For non-life *firms* the *MCR* represents the *minimum capital requirement* (or margin of solvency) prescribed by the *Insurance Directives*. ...~~
- ...
- ...
- The premiums amount

- 1.1.45 R The *premiums amount* is:
- (1) 18% of the *gross adjusted premiums amount*; less 2% of the amount, if any, by which the *gross adjusted premiums amount* exceeds €61.3 ~~£53.5~~ million; multiplied by

...

...

The claims amount

- 1.1.47 R The claims amount is:
- (1) 26% of the *gross adjusted claims amount*; less 3% of the amount, if any, by which the *gross adjusted claims amount* exceeds €42.9 ~~£37.5~~ million; multiplied by

...

...

- 1.1.49 G (1) ~~Under the *Insurance Directives* the Euro amounts specified in *INSPRU* 1.1.45R(1) and *INSPRU* 1.1.47R(1) are subject to annual review. The relevant amounts will be increased by the percentage change in the European index of consumer prices (comprising all *EU* member states, as published by Eurostat) from 20 March 2002, to the relevant review date, rounded up to a multiple of €100,000, provided that where the percentage change since the last increase is less than 5%, no increase will take place. [deleted]~~
- (2) ~~No provision for the index linking of these amounts is made by the *Reinsurance Directive*. However, to ensure consistency as between *pure reinsurers*, *mixed insurers* and other *insurers*, the *FSA* intends to amend the Euro amounts specified in *INSPRU* 1.1.45 R(1) and *INSPRU* 1.1.47R(1) for all such *firms* when an index linked increase is required by the *Insurance Directives*. [deleted]~~

- 1.1.50 R ~~For the purposes of *INSPRU* 1.1.45R(1) and *INSPRU* 1.1.47R(1), the exchange rate from the Euro to the pound sterling for each year beginning on 31 December is the rate applicable on the last day of the preceding October for which the exchange rates for the currencies of all the European Union member states were published in the Official Journal of the European Union. [deleted]~~

...

Accounting for premiums and claims

- 1.1.66 R For the purposes of *INSPRU* 1.1.54R, *INSPRU* 1.1.56R, *INSPRU* 1.1.60R and *INSPRU* 1.1.62R, amounts of *premiums* and *claims* must be:

- (1) determined in accordance with the *insurance accounts rules* ~~or the Friendly Societies (Accounts and Related Provisions) Regulations 1994~~, as appropriate;

...

...

- 1.1.71 R Where there has been a significant change in the business portfolio of the *firm* since the end of the *financial year in question*, for example, a line of business has been transferred to another *firm*, or the *firm* no longer carries on a particular *class of insurance business*, the *gross adjusted premiums amount* and the *gross adjusted claims amount* must both be recalculated to take into account the impact of this change. The recalculation must take into account the requirements of the *insurance accounts rules* ~~or the Friendly Societies (Accounts and Related Provisions) Regulations 1994~~, as appropriate.

...

Enhanced capital requirement for general insurance business

- 1.1.72A G This section sets out the requirement for *Solvency I firms* carrying on *general insurance business*, ~~other than non-directive insurers~~, to calculate their *ECR*. ...
- 1.1.72B R A *Solvency I firm* carrying on *general insurance business*, ~~other than a non-directive insurer~~, must calculate the amount of its *ECR*.
- 1.1.72C R A *firm* to which *INSPRU 1.1.72BR* applies must calculate its *ECR* in respect of its *general insurance business* as the sum of:
- (1) the *asset-related capital requirement*; and
 - (2) the *insurance-related capital requirement*; ~~less~~.
 - (3) ~~the firm's equalisation provisions~~. [deleted]

...

INSPRU 1.1.93R to *INSPRU 1.1.96* are deleted in their entirety. The deleted text is not shown.

1.2 Mathematical reserves

Application

- 1.2.1 R *INSPRU 1.2* applies to a *long-term insurer* unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

Purpose

- 1.2.3 G This section applies to all *firms* carrying on *long-term insurance business* and implements some of the requirements contained in article 20 of the *Consolidated Life Directive*. The implementation is designed to ensure that a *firm's mathematical reserves* in respect of *long-term insurance contracts* meet the minimum requirements set by the *Consolidated Life Directive*. A *firm* may use a prospective or a retrospective method to value its *mathematical reserves* (see *INSPRU 1.2.7R*).

...

Negative mathematical reserves

...

- 1.2.25A G ~~In addition, the *Consolidated Life Directive* requires that no contract should be valued at less than its guaranteed *surrender value* (see *INSPRU 1.2.62AG*). As a result, no contract with a guaranteed *surrender value* to which the *Consolidated Life Directive* applies should be valued as if it were an asset. Although the *Reinsurance Directive* does not require this treatment of contracts with guaranteed *surrender values* to be applied to *pure reinsurers*, the *FSA's* policy is that there should be equal treatment in this respect. *INSPRU 1.2.62R* makes further provision relating to the *mathematical reserves* to be established in respect of such contracts where the *surrender value* is guaranteed. When considering the impact that the amount payable on surrender may have on the valuation of a contract, a *firm* should have regard to *INSPRU 1.2.71R*.~~

...

Application of *INSPRU 1.2* to Lloyd's

- 1.2.92 R ~~*INSPRU 1.2* applies to *managing agents* in accordance with *INSPRU 8.1.4R*. [deleted]~~

Approved reinsurance to close

- 1.2.93 R ~~In respect of business that has been subject to an *approved reinsurance to close*, *managing agents* must calculate *mathematical reserves* (before and after deduction of reinsurance cessions) for the reinsuring and not for the reinsured *member*. [deleted]~~

...

INSPRU 1.4 is deleted in its entirety. The deleted text is not shown.

1.5 Internal-contagion risk

Application

...

1.5.2 R *INSPRU 1.5* does not apply, to the extent stated, to any *insurer* in (1) to (4):

(1) none of the provisions apply to:

(a) *non-directive friendly societies*; or

(b) *UK Solvency II firms*; or

(c) *firms which qualify for authorisation under Schedule 3 of the Act*;

(2) none of the provisions, apart from *INSPRU 1.5.33R* (payment of financial penalties) apply to *firms* which qualify for authorisation under Schedule 3 or 4, but not under Schedule 3, of the *Act*;

(3) ...

(4) *INSPRU 1.5.41R* to *INSPRU 1.5.57R* (*UK branches* of certain *non-EEA insurers*) do not apply to:

(a) ~~*UK insurers*~~ whose head office is in the United Kingdom; or

(b) ...

1.5.3 G ~~The scope of application of *INSPRU 1.5* is not restricted to *firms* that are subject to the relevant *EU* directives. [deleted]~~

...

Purpose

1.5.8 G ... Requirements relevant to ~~*group* contagion risk~~ are set out in ~~*INSPRU 6*~~.

...

Restriction of business

...

1.5.13 R ...

(2) ~~(1) does not prevent a *friendly society* which was on 15 March 1979 carrying on *long term insurance business* from continuing to carry~~

~~on savings business. [deleted]~~

...

Permissions not to include both types of insurance

1.5.17 G ...

- (3) It is *FSA* policy, ~~in compliance with EU directives on insurance,~~ not to grant or vary *permission* if that would allow a newly established *firm*, or an existing *firm* engaging solely in *general insurance business* or solely in *long-term insurance business*, to engage in both *general insurance business* and *long-term insurance business*. This does not apply where a *firm's permission* to carry on *long-term insurance business* is or is to be restricted to *reinsurance*. It also does not apply where a *firm's permission* to carry on *general insurance business* is or is to be restricted to *effecting or carrying out accident or sickness contracts of insurance* (~~see article 18(2) of the Consolidated Life Directive~~).
- (4) Where a *firm's permission* extends to *effecting or carrying out life and annuity contracts of insurance* this will normally include *permission* to *effect or carry out accident contracts of insurance* or *sickness contracts of insurance* on a supplementary basis (~~see article 2(1)(e) of the Consolidated Life Directive~~).

...

Payment of financial penalties

...

1.5.34 G ~~INSPRU 1.5.2R states that this provision applies to all firms, except mutuals, and includes firms qualifying for authorisation under Schedule 3 or 4 to the Act. [deleted]~~

...

INSPRU 1.5.58R to INSPRU 1.5.60R are deleted in their entirety. The deleted text is not shown.

...

2 Credit risk in insurance

2.1 Application

2.1.1 R *INSPRU* 2.1 applies to an *insurer* unless it is:

...

- (3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

2.1.22 R ...

(4) In (3) a *firm's* business amount means the sum of:

...

(c) such amount as the *firm* may select not exceeding, ~~in the case of a *firm* which is not a *participating insurance undertaking*, the amount of the *firm's* total capital after deductions as calculated at stage M of the *capital resources table* or, in the case of a *firm* which is a *participating insurance undertaking*, the amount calculated in accordance with (5A) or, in either case, if higher:~~

- (i) in the case of a *firm* carrying on *general insurance business*, the amount of its *general insurance capital requirement*; and
- (ii) in the case of a *firm* carrying on *long-term insurance business*, the amount of its *long-term insurance capital requirement* and, where it is a *regulatory basis only life firm*, the amount of its *resilience capital requirement*.

(5) ...

(5A) ~~For the purpose of (4)(c), a *firm* which is a *participating insurance undertaking* must calculate the amount of the *firm's group capital resources* less the difference between:~~

- (a) ~~the *firm's group capital resources requirement*; and~~
- (b) ~~the *firm's capital resources requirement*. [deleted]~~

...

INSPRU 2.1.42R to INSPRU 2.1.49R are deleted in their entirety. The deleted text is not shown.

2.2 Asset-related Capital Requirement

Application

2.2.1 R *INSPRU 2.2* applies to an *insurer* unless it is:

...

(5) an *incoming Treaty firm*; or

(6) a *UK Solvency II firm*.

2.2.2 G ~~The scope of application of *INSPRU 2.2* is not restricted to *firms* that are subject to relevant *EU directives*. [deleted]~~

2.2.3 R *INSPRU 2.2* applies to a *firm* only in relation to its *general insurance business*.

...

Purpose

...

2.2.7 G The *FSA* will use the *enhanced capital requirement* as the benchmark for *individual capital guidance* for a *Solvency I firm* carrying on *general insurance business*, ~~other than a *non-directive insurer*~~. The *enhanced capital requirement* is the sum of the *asset-related capital requirement* and the *insurance-related capital requirement* ~~less the *firm's equalisation provisions*~~. This section sets out *rules and guidance* relating to the *asset-related capital requirement*. *Rules and guidance* relating to the *insurance-related capital requirement* are set out in *INSPRU 1.1*.

...

Application of *INSPRU 2.2* to Lloyd's

2.2.17 R ~~*INSPRU 2.2* applies to *managing agents* and to the *Society* in accordance with:~~

(1) ~~for *managing agents*, *INSPRU 8.1.4R*; and~~

(2) ~~for the *Society*, *INSPRU 8.1.2R* [deleted]~~

2.2.18 R ~~This chapter applies to the *Society* for each *member*, including the capital charge relating to *central assets*, to the extent that those assets are held to support a particular *member*. [deleted]~~

3 Market risk

3.1 Market risk in insurance

3.1.1 R *INSPRU 3.1* applies to an *insurer*, unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

Purpose

...

3.1.7 G *INSPRU 3.1* addresses the impact of *market risk* on *insurance business* in the ways set out below:

...

(6) ~~The *Reinsurance Directive* *INSPRU 3.1.61AR* applies to *pure reinsurers* "prudent person" investment principles in relation to the investment of their assets. *INSPRU 3.1.61AR* sets out these principles.~~

...

3.1.53 R (1) Subject to *INSPRU 3.1.53R*, a *firm* must hold *admissible assets* in each currency of an amount equal to at least 80% of the amount of its liabilities in that currency arising under or in connection with *contracts of insurance* ~~(but excluding, for a *firm* that carries on *general insurance business*, any *non-credit equalisation provision*),~~ except where the amount of those assets does not exceed 7% of the assets in other currencies.

(2) ...

3.1.53A G ~~For the purpose of *INSPRU 3.1.53R*, a *firm* may allocate the total *credit equalisation provisions* to different currencies in proportion to the split by currency of the *technical provisions* for *credit insurance business* established in accordance with *GENPRU 1.3.4R*. Alternatively, another allocation which the *firm* is able to justify as broadly appropriate may be used. [deleted]~~

...

INSPRU 3.1.62R to *INSPRU 3.1.66R* are deleted in their entirety. The deleted text is not shown.

3.2 Derivatives in insurance

3.2.1 R This section applies to an *insurer*, unless it is:

- (1) a *non-directive friendly society*; or
- (2) an *incoming EEA firm*; or

(3) an *incoming Treaty firm*; or

(4) a *pure reinsurer*; or

(5) a UK Solvency II firm.

3.2.2 G ~~The scope of application of *INSPRU 3.2* is not restricted to *firms* that are subject to the relevant *EU* directives. [deleted]~~

...

Application of *INSPRU 3.2* to Lloyd's

3.2.43 R ~~*INSPRU 3.2* applies to *managing agents* and to the *Society* in accordance with:~~

(1) ~~for *managing agents*, *INSPRU 8.1.4R*; and~~

(2) ~~for the *Society*, *INSPRU 8.1.2R*. [deleted]~~

4 Liquidity risk management

4.1 Application

...

4.1.4 R This section does not apply to:

(1) a *non-directive friendly society*; or

(2) an *incoming EEA firm*; or

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

Application of *INSPRU 4.1* to Lloyd's

4.1.69G G ~~*INSPRU 4.1* applies to *managing agents* and to the *Society* in accordance with:~~

(1) ~~for *managing agents*, *INSPRU 8.1.4R*; and~~

(2) ~~for the *Society*, *INSPRU 8.1.2R* [deleted]~~

4.1.70 G ~~In accordance with *INSPRU 8.6.2R*, the rules and guidance in *INSPRU 4.1* relating to the establishment and maintenance of a business plan do not apply to the *Society*. [deleted]~~

5 Operational Risk Management

5.1 Application

5.1.1 G *INSPRU* 5.1 applies to an *insurer* unless it is:

...

(3) an *incoming Treaty firm*; or

(4) a UK Solvency II firm.

...

Application of *INSPRU* 5.1 to Lloyd's

5.1.24 G ~~*INSPRU* 5.1 applies to *managing agents* and to the *Society* in accordance with:~~

(1) ~~for *managing agents*, *INSPRU* 8.1.4R; and~~

(2) ~~for the *Society*, *INSPRU* 8.1.2R [deleted]~~

5.1.25 G ~~In accordance with *INSPRU* 8.5.2GR, the *rules* and *guidance* in *INSPRU* 5.1 relating to the establishment and maintenance of a business plan do not apply to the *Society*. [deleted]~~

INSPRU 6.1 is deleted in its entirety. The deleted text is not shown.

...

7 Individual Capital Assessment

7.1 Application

7.1.1 R *INSPRU* 7.1 applies to an insurer unless it is:

...

(5) an *incoming Treaty firm*; or

(6) a UK Solvency II firm

7.1.2 R ~~Subject to *INSPRU* 7.1.3R, *INSPRU* 7.1 applies to *managing agents* and to the *Society* in accordance with:~~

(1) ~~for *managing agents*, *INSPRU* 8.1.4R; and~~

(2) ~~for the Society, INSPRU 8.1.2R. [deleted]~~

7.1.3 R ~~Managing agents must carry out assessments of capital adequacy for each syndicate they manage by reference to all open syndicate years taken together. [deleted]~~

...

7.1.9B G The requirements and *guidance* in this section are drafted so as to apply to a *firm* on a solo basis. ~~As noted in GENPRU 1.2.17G, however, in some cases the requirements in GENPRU 1.2 apply on a consolidated basis. In these cases, a firm should read and apply this section making appropriate adjustments to reflect the application of the GENPRU 1.2 requirements on a consolidated basis.~~

...

INSPRU 7.1.74G to INSPRU 7.1.90R are deleted in their entirety. The deleted text is not shown.

FSA assessment process - all firms

...

7.1.99 G ... ~~The FSA will not grant a waiver that would cause a breach of the minimum capital requirements under the *Insurance Directives* or *Reinsurance Directive*.~~

...

INSPRU 8 is deleted in its entirety. The deleted text is not shown.

Transitional provisions

TP 1 Application

1.1 R INSPRU TP 1 applies to an insurer unless it is:

...

(3) ~~an incoming Treaty firm; or~~

(4) ~~a UK Solvency II firm.~~

...

3 **PRU waivers**

Application

3.1 R *INSPRU* TP 3 applies to an *insurer* unless it is

...

(3) an *incoming Treaty firm*; or

(4) a *UK Solvency II firm*.

...

4 ~~EEA pure reinsurers~~ [deleted]

This table is deleted in its entirety.

5 ~~Pure reinsurance groups~~ [deleted]

This table is deleted in its entirety.

Notification and reporting requirements

Sch 2 Notification and reporting requirements

...

Sch 2.3 G Table

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...				
<i>INSPRU</i> 3.1.65R [deleted]	<i>Syndicate liabilities not covered by matching syndicate assets as required by INSPRU 3.1.53R</i>	Nature and extent of <i>syndicate liabilities not covered by matching syndicate assets as required by INSPRU 3.1.53R</i>	<i>Syndicate liabilities are no longer covered by matching syndicate assets as required by INSPRU 3.1.53R</i>	Immediately
<i>INSPRU</i> 6.1.43BR [deleted]	Intention of a <i>group undertaking</i> to issue a <i>capital</i>	Fact of intention and details of intended amount, issue	Intention to issue	As soon as proposed issue becomes known to

	<i>instrument for inclusion in group capital resources</i>	date, type of investor, stage of capital, features of instrument and confirmation of compliance with <i>rules</i>		<i>firm</i>
<i>INSPRU 6.1.43CR</i> [deleted]	Proposed changes to details of the issue of a <i>capital instrument</i> notified under <i>INSPRU 6.1.43BR</i>	Proposed change and all information required under <i>INSPRU 6.1.43BR(1)</i> to <i>INSPRU 6.1.43BR(4)</i>	Intention to change any details of the issue previously notified to the <i>FSA</i>	As soon as the changes are proposed
<i>INSPRU 6.1.43DR</i> [deleted]	Proposed establishment of a debt securities program by a <i>group undertaking</i>	All information required by <i>INSPRU 6.1.43BR(1)</i> to <i>INSPRU 6.1.43BR(4)</i>	Intention to establish	As soon as proposed establishment becomes known to <i>firm</i>
<i>INSPRU 6.1.43FR</i> [deleted]	Issue of <i>capital instruments</i> by a <i>group undertaking</i> under <i>INSPRU 6.1.43ER</i>	All information required under <i>INSPRU 6.1.43BR(1)</i> to <i>INSPRU 6.1.43BR(3)</i> and confirmation that no changes have been made to the terms of the instrument since the previous issue of a similar instrument	Intention to issue	No later than date of issue
<i>INSPRU 7.1.83R</i> [deleted]	<i>Syndicate ICA</i> and <i>balancing amount</i> in respect of	<i>Syndicate ICA</i> and <i>balancing amount</i> in respect of each <i>syndicate</i>	Notification should be made periodically	As part of the annual capital-setting process, in

	each <i>syndicate</i>			good time for the <i>Society</i> to review and place appropriate reliance on them when determining capital assessments for each <i>member</i>
<i>INSPRU</i> 7.1.89R [deleted]	Significant doubt about the adequacy of a <i>syndicate ICA</i> or <i>balancing amount</i> with respect to <i>syndicate</i> risks and controls	Revised <i>syndicate ICA</i> and <i>balancing amount</i>	The <i>managing agent</i> considers that <i>syndicate ICA</i> and <i>balancing amount</i> communicated in the capital setting process are no longer adequate in the light of the risks to which the <i>syndicate</i> business is exposed	Immediately
<i>INSPRU</i> 8.2.17R [deleted]	Information the <i>managing agent</i> has concerning material risks to <i>funds at Lloyd's</i> or <i>central assets</i>	All information concerning relevant risk	Receipt of information	As soon as possible
<i>INSPRU</i> 8.2.23R [deleted]	Intention to approve the form of any new <i>Lloyd's trust deed</i>	Fact of intention	Intention to approve	As soon as practical
<i>INSPRU</i> 8.2.24R [deleted]	Intention to make any amendment which may alter the meaning or effect of any <i>byelaw</i>	Fact of intention	Intention to amend	As soon as practical

	(including <i>Lloyd's trust deeds</i> , standard form letters of credit and guarantees)			
<i>INSPRU</i> 8.2.25R [deleted]	Full details of form of new <i>Lloyd's trust deed</i> or amendments to <i>byelaw</i> (including <i>Lloyd's trust deeds</i> , standard form letters of credit and guarantees)	(1) Statement of purpose of amendment or new form and expected impact, if any, on <i>policyholders</i> , <i>managing agents</i> , <i>members</i> and potential <i>members</i> , and (2) Description of the consultation undertaken and summary of significant responses to consultation	Not specified	Normally not less than three months in advance of proposed change

...

Sch 6 Rules that can be waived

- G The rules in *INSPRU* can be waived by the *FSA* under section 148 of the *Act* (Modification or waiver of rules), except for *INSPRU* 9.1.1R (Actions for damages). However, if the *rules* incorporate requirements laid down in European directives, it will not be possible for the *FSA* to grant a *waiver* that would be incompatible with the *United Kingdom's* responsibilities under those directives. It therefore follows that if a *rule* in *INSPRU* contains provisions which derive partly from a directive, and partly not, the *FSA* will be able to consider a *waiver* of the latter requirements only, unless the directive provisions are optional rather than mandatory.

Annex I

Amendments to the Prudential sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries (MIPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text.

2 Insurance mediation activity: responsibility, knowledge, ability and good repute

2.3 Knowledge, ability and good repute

...

- 2.3.5 G *Firms* are reminded that *Principle 3* requires firms to take reasonable care to organise and control their affairs responsibly and effectively. *Principle 3* is amplified by the *rule* which requires firms to take reasonable care to establish and maintain such systems and controls as are appropriate to its business (including SYSC 3.1.1R and SYSC 4.1.1R). A *firm's* systems and controls should enable it to satisfy itself of the suitability of anyone who acts for it (including SYSC 3.2.13G and SYSC 5.1.2G). This includes the assessment of an individual's honesty and competence. In addition, the competent employees rule (including SYSC 3.1.6R and SYSC 5.1.1R) sets out a high-level competence requirement which every *firm* should follow.

...

Annex J

Amendments to the Prudential sourcebook for UCITS Firm (UPRU)

In this Annex, underlining indicates new text and striking through indicates deleted text.

2 Prudential requirements

2.2 Method of calculation of financial resources

2.2.1 R ...

PART II DETAILED REQUIREMENTS

...

11 Illiquid assets (Item 15)

...

- (i) if not otherwise covered, any holding in eligible capital instruments of an ~~insurance undertaking~~ insurance undertaking, insurance holding company, or ~~reinsurance undertaking~~ reinsurance undertaking that is a *subsidiary* or *participation*. Eligible capital instruments include ordinary share capital, ~~cumulative~~ preference shares, perpetual securities and long-term subordinated loans, that are eligible for ~~insurance undertakings~~ insurance undertakings under *GENPRU 2* or, as the case may be, *INSPRU 7* in the case of an insurer that is not a *Solvency II undertaking* or *SOLPRU 3* in the case of a *Solvency II undertaking* or the *Society*.

...

Annex K

**Amendments to the Interim Prudential Sourcebook for Friendly Societies
(IPRU(FSOC))**

Note to reader: The Euro amounts in this Annex are based on the version of IPRU(FSOC) as proposed to be amended in the Quarterly Consultation Paper No. 33 (CP 12/11) published on 6 June 2012 which is intended to come into force on 31 December 2012.

In this Annex, underlining indicates new text and striking through indicates deleted text.

THE PURPOSE OF THE PRUDENTIAL RULES FOR FRIENDLY SOCIETIES AND AN OVERALL DESCRIPTION

...

7 Chapter 3 focuses on systems and controls. *Friendly societies* should also refer to the provisions on senior management arrangements, systems and controls in the High Level Standards part of the Handbook (SYSC) and to Annex 3 of *IPRU(FSOC)*. *Directive friendly societies* should also refer to SOLPRU 9.

...

15 *FSA* guidance is set out in the Annexes and *friendly societies* may also wish to refer to the guidance in SOLPRU, *IPRU(INS)*, *GENPRU* and *INSPRU*.

...

Chapter 1

Application

...

1.1A The rules in Chapters 1, 2 (with the exception of rule 2.3(1)(a) in relation to *registered branches*), 3 (with the exception of rule 3.1(7)), rule 4.20, rule 5.1A, Chapters 7 and 8 also apply to a *directive friendly society* which has permission under the *Act* to *effect or carry out contracts of insurance*. A *directive friendly society* must also comply with any requirement imposed on it by or under the *Act*, the *1992 Act* or the *1974 Act*.

...

Chapter 2

INTEGRITY, SKILL, CARE AND DILIGENCE

Legal Compliance

- 2.1 *A friendly society* must take reasonable steps to ensure that –
- (a) it does not carry on activities beyond its powers;
 - (b) it and its *registered branches* comply with –
 - (i) any requirements of or under the *1992 Act* or the *Act* which relate to the conduct of its *insurance business*, and
 - (ii) any applicable requirement (whether of the law of any part of the United Kingdom or of the law of another *EEA State*) which gives effect to the *insurance Directives Solvency II Directive* or is otherwise applicable to the insurance activities of the *friendly society*.

...

Chapter 4

FINANCIAL PRUDENCE

...

Minimum guarantee fund: long-term insurance business

- 4.5 (1) [deleted]
- (2) For a *non-directive incorporated friendly society*, in the *financial year* during which the *friendly society* first obtains permission under the *Act* to carry on *long-term insurance business*, the *minimum guarantee fund* is the amount in column 2 of the table, which corresponds to the *friendly society's annual contribution income* in respect of that business in the last preceding *financial year*, as shown in column 1 of the table.

Contribution Income (in Euro <u>pound sterling</u>)	Minimum guarantee fund (in Euro <u>pound sterling</u>)
1,000,000 <u>875,000</u> or less	115,000 <u>100,000</u>
1,000,001 – 1,500,000 <u>875,001 – 1,300,000</u>	230,000 <u>200,000</u>
1,500,001 – 2,000,000 <u>1,300,001 – 1,750,000</u>	350,000 <u>302,000</u>
2,000,001 – 2,500,000 <u>1,750,001 – 2,200,000</u>	460,000 <u>405,000</u>
2,500,001 – 3,000,000 <u>2,200,001 – 2,625,000</u>	580,000 <u>508,000</u>
3,000,001 <u>2,625,001</u> or more	700,000 <u>611,000</u>

But where the *friendly society* had no *annual contribution income* in respect of *long-term insurance business* in the last preceding *financial year* or has not been in existence long enough to have a preceding *financial year*, the

minimum guarantee fund is ~~115,000 Euro~~ 100,000 pound sterling.

...

- (4) Where a *non-directive incorporated friendly society* obtains permission under the *Act* (or has obtained permission under the *Act* or authorisation under its predecessor legislation) to carry on *long-term insurance business*-
- (a) of a *class* additional to that in respect of which it already has permission; or
- (b) in a part of the United Kingdom additional to that in respect of which it already has permission,

a *minimum guarantee fund* of ~~700,000 Euro~~ 611,000 pound sterling must be maintained by that *friendly society* for the whole of its *long-term insurance business* (that is to say, not only for the additional business carried on but also for the business previously carried on).

Minimum guarantee fund: long-term insurance business

- 4.6 (1) [deleted]
- (2) For *non-directive incorporated friendly societies*, the *minimum guarantee fund* for *general insurance business* is ~~260,000 Euro~~ 227,000 pound sterling.

...

Valuation of solvency margins

- 4.7 ...
- (3) The items which relate to future surpluses, *zillmerising* and hidden reserves (referred to as implicit items) must be treated as having no value. A *friendly society* which applies for a waiver of this rule under section 148 of the *Act* with respect to future profits must submit with the application for waiver:
- (a) an actuarial report substantiating the likelihood of the emergence of the future profits in the future; ~~and~~
- (b) ~~a plan as to how it intends to comply with the future limits on, and termination of use of, implicit items for future profits required by the Life Directive (2002/83/EC).~~ [deleted]

...

- (7) ~~For the purposes of the rules in Chapter 4 and the definition of *non-directive friendly society*, the exchange rate from the Euro to the pound sterling for each year beginning on 31 December is the rate applicable on the last day of the preceding October for which the exchange rates for the currencies of all the European Union member states were published in the Official Journal of~~

the European Union. ~~[deleted]~~

...

Chapter 5

PRUDENTIAL REPORTING

Annual actuarial investigation

...

- 5.1A (1) ~~A directive friendly society~~ must comply with rules 9.1 to 9.36, 9.37, and 9.39 of *IPRU(INS)* as if references to an *insurer* in those rules included a ~~directive friendly society~~. ~~[deleted]~~
- (2) In relation to a *directive friendly society*, references in Form 13, 14, and 15 in Appendix 9.1 of *IPRU(INS)* to the *insurance accounts rules* must be taken as referring to the *Accounts Regulations*. ~~[deleted]~~

...

Appendix 2

GENERAL INSURANCE BUSINESS SOLVENCY MARGIN

Part I: the Premiums Basis

...

4. If the amount arrived at under 3 is more than ~~61.3 million Euro~~ 53.5 million pound sterling, it must be divided into two portions, the former consisting of ~~61.3 million Euro~~ 53.5 million pound sterling and the latter comprising the excess.

...

18. If the amount arrived at under 17 is more than ~~42.9 million Euro~~ 37.5 million pound sterling, it must be divided into two portions, the former consisting of ~~42.9 million Euro~~ 37.5 million pound sterling and the latter comprising the excess.

...

Appendix 10

Prudential Reporting Forms

...

FSC 3 – FORM 11 (Sheet 1)

Division of Sub-total A	Other than health insurance	Up to and including sterling equivalent of 61.3 M Euro £53.5M x 18/100
		Excess (if any) over 61.3 M Euro £53.5 M x 16/100
	Health insurance	Up to and including sterling equivalent of 61.3 M Euro £53.5M x 6/100
		Excess (if any) over 61.3 M Euro £53.5M x 16/300

...

Division of Sub-total H	Other than health insurance	Up to and including sterling equivalent of 61.3 M Euro £53.5 M x 18/100
		Excess (if any) over 61.3 M Euro £53.5 M x 16/100
	Health insurance	Up to and including sterling equivalent of 61.3 M Euro £53.5 M x 6/100
		Excess (if any) over 61.3 M Euro £53.5 M x 16/300

¹Entries in column 2, lines 17-20 and 28-31 must be the corresponding entries in column 1 of the Form for the previous year, even if the amount of Euro in the description of the line has changed.

...

FSC 3 – FORM 12

Returns under the Friendly Societies Prudential Rules

General insurance business: Calculation of required margin of solvency – second method, and statement of required minimum margin

Name of Society

Period ended 31 December

	Reg No	Units £/£000

Name of Fund/Summary

	1 Last 12 months of this period	2 Last 12 months of the previous period
--	---------------------------------	---

...

Division of Sub-total F	Other than health insurance	Up to and including sterling equivalent of 42.9 M Euro <u>£37.5 M</u> x 26/100 (note 3)
		Excess (if any) over 42.9 M Euro <u>£37.5 M</u> x 23/100 (note 3)
	Health insurance	Up to and including sterling equivalent of 42.9 M Euro <u>£37.5 M</u> x 26/300 (note 3)
		Excess (if any) over 42.9 M Euro <u>£37.5 M</u> x 23/300 (note 3)

NOTES

1. If the society has not been in existence long enough to acquire a reference period, this must be stated and lines 11 to 41 ignored.
2. The entry at line 42 must be equal to the entry at line 52 on Form 11.
3. Entries in column 2, lines 32-35 must be the corresponding entries in column 1 of the Form for the previous year, even if the amount of ~~Euro~~ in the description of the line has changed.

...

Annex 4**GUIDANCE ON MARGINS OF SOLVENCY AND THE GUARANTEE FUND**

...

The required margin of solvency

...

- 4A ~~Guidance in GENPRU 2 Annex 8G (Guidance on applications for waivers relating to implicit items) is relevant to friendly societies applying for a waiver of rule 4.7(3) of IPRU(FSOC) under section 148 of the Act (Modification or waiver of rules):⁴⁰ [deleted]~~

...

Minimum requirements

- 7 Chapters 4 and 5 ~~which are based on the insurance Directives~~, set out the current solvency and valuation requirements for friendly societies carrying on *insurance business*. Rules of this type cannot take into account the individual needs of a particular *friendly society*, but should be regarded as an absolute minimum requirement which will be supplemented by explicit or implicit margins on the advice of the actuary.

...

Non-Directive Incorporated Friendly Societies

...

Long term business

- 11.4 (1) These may fall outside the EC requirements but fall within the scope of rule 5.1 and are required to be valued annually. The *required margin of solvency* is set out in rules 4.1 to 4.7. New *friendly societies* should have *margins of solvency* at least equal to the appropriate *minimum guarantee fund*. Rule 4.5 specifies a *minimum guarantee fund* with a threshold of ~~100,000 Euro~~ 100,000 pound sterling increasing in steps. This may be varied by the exercise of the *FSA's* power under section 148 of the *Act*.

...

General insurance business

- 11.5 Similar considerations will apply in the case of *non-directive incorporated friendly societies* carrying on *general insurance business*. The *minimum*

guarantee fund is ~~225,000 Euro~~ 227,000 pound sterling. These societies are required to be valued triennially.

Annex L

Amendments to the Interim Prudential sourcebook: Insurers (IPRU(INS))

Note to reader: The Euro amounts in this Annex are based on the version of IPRU(INS) as proposed to be amended in the Quarterly Consultation Paper No. 33 (CP 12/11) published on 6 June 2012 which is intended to come into force on 31 December 2012.

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

CONTENTS**VOLUME ONE**

...

Chapter 9 Financial reporting

...

Part V ~~Group Capital Adequacy~~ [deleted]

...

Part VII ~~Lloyd's of London~~ [deleted]

...

VOLUME TWO

...

Appendix 9.2 General insurance business: revenue account and additional information (Forms 20A and 20 - ~~39 36~~) (rules 9.14 to ~~9.22 9.21~~)

...

Appendix 9.7 ~~Insurance statistics: other EEA states (Forms 91 to 94) (rule 9.37)~~ [deleted]

...

Appendix 9.9 ~~Group Capital Adequacy (rule 9.40 to rule 9.42 and guidance 9.43)~~ [deleted]

...

Appendix 9.12 ~~Certificate by the Council (rule 9.58 (1)(a))~~ [deleted]

Appendix 9.13	Statement by the Lloyd's actuary (rule <i>IPRU(INS)</i> 9.58 (1)(b)) <u>[deleted]</u>
Appendix 9.14	Certificate by syndicate actuary (rule <i>IPRU(INS)</i> 9.58 (1)) <u>[deleted]</u>
Appendix 9.15	Auditor's report (rule <i>IPRU(INS)</i> 9.58(3)) <u>[deleted]</u>
Appendix 9.16	Accounting classes (rule <i>IPRU(INS)</i> 9.49(1)(b)) <u>[deleted]</u>
Appendix 9.17	Accounting Records <u>[deleted]</u>
Appendix 9.18	Auditors' Report <u>[deleted]</u>

...

Chapter 1

APPLICATION RULE

CONTENTS

Application

...

1.2 ~~The Society of Lloyd's~~ [deleted]

...

Chapter 1

APPLICATION RULE

Application

Insurers

- 1.1 An insurer must comply with *IPRU(INS)* unless it is -
- (a) a *friendly society*¹; or
 - (b) an *EEA insurer* or an *EEA pure reinsurer* qualifying for authorisation under Schedules 3 or 4 to the Act; or
 - (c) a UK Solvency II firm.

¹ A *non-directive friendly society* must comply with *IPRU(FSOC)*; a *directive friendly society* must comply with ~~*GENPRU* and *INSPRU SOLPRU*~~; and with Chapters 1, 2 (with the exception of rule 2.3(1)(a) in relation to *registered branches*), and 3, 4 (rules 4.20 to 4.23 only), 5 (rule 5.1A only) 7, and 8 and Appendix 3 of *IPRU(FSOC)*. Rule 5.1A of *IPRU(FSOC)* effectively applies most of Chapter 9 of *IPRU(INS)* to *directive friendly societies*, notwithstanding *IPRU(INS)* 1.1(a)

~~The Society of Lloyd's~~

- 1.2 ~~No provisions of *IPRU(INS)* apply to the *Society of Lloyd's*, or *members* of the *Society of Lloyd's* except rules 9.37 and 9.38, and Part VII of Chapter 9. [deleted]~~

...

Chapter 9

FINANCIAL REPORTING

Part I

ACCOUNTS AND STATEMENTS

...

9.15 ...

- (2) For the purposes of this rule and rules 9.17(1); and 9.19(1) and 9.22(2), business must be taken to be *accounted for* on an **underwriting year basis** where it relates to risks -

...

Additional information on general insurance business (claims equalisation provisions)

- 9.22 (1) ~~This rule applies to non-credit *insurance business* as defined in *INSPRU* 1.4.11R(1) and credit *insurance business* as defined in *INSPRU* 1.4.38R.~~
- (2) ~~An insurer to which *INSPRU* 1.4.11R to *INSPRU* 1.4.37G apply (unless *INSPRU* 1.4.18R applies) and an insurer to which *INSPRU* 1.4.43R applies (unless *INSPRU* 1.4.44R applies) must, in accordance with the requirements of **Appendix 9.2**, prepare –~~
- (a) ~~**Form 37**;~~
- (b) ~~**Form 38** for *general insurance business* accounted for on an 'accident year basis'; and~~
- (c) ~~**Form 39** for *general insurance business* accounted for on an 'underwriting year basis'. [deleted]~~

...

Provisions supplemental to rules 9.25 to 9.27

...

9.28 ...

- (6) ~~Rules 9.25(2), 9.26(1)(a) to (e) and 9.27 apply in relation to the members of the *Society* taken together as they apply in relation to an *insurer* and in relation to the members of the *Society* (1) to (4) of this rule do not apply.~~
[deleted]

...

Part III is deleted in its entirety. The deleted text is not shown.

...

Part V is deleted in its entirety. The deleted text is not shown.

...

Part VII is deleted in its entirety. The deleted text is not shown.

...

ANNEX 11.1**CLASSES OF LONG-TERM INSURANCE BUSINESS**

...

VIII	Collective insurance etc	Effecting or carrying out contracts of a kind referred to in Article 2(2)(e) of the Consolidated Life Directive <u>article 2(3)(b)(v) of the <i>Solvency II Directive</i></u> .
IX	Social insurance	Effecting or carrying out contracts of a kind referred to in Article 2(3) of the Consolidated Life Directive <u>article 2(3)(c) of the <i>Solvency II Directive</i></u> .

...

Chapter 12**TRANSITIONAL ARRANGEMENTS**

...

Pure reinsurance groups

- 12.5A ~~A pure reinsurer whose ultimate EEA insurance parent undertaking is the parent undertaking of a group comprised solely of reinsurance undertakings need not~~

~~comply with rule 9.40 (Group capital adequacy) before 10 December 2007.~~
~~[deleted]~~

...

VOLUME TWO

Appendices to the Rules

CONTENTS

...

Appendix 9.2 General insurance business: revenue account and additional information
 (Forms 20A and 20 - ~~39 36~~) (rules 9.14 to ~~9.22 9.21~~)

Appendix 9.7 ~~Insurance statistics: other EEA states (Forms 91 to 94) (rule 9.37) [deleted]~~

...

Appendix 9.9 ~~Group Capital Adequacy (rule 9.40 to rule 9.42 and guidance 9.43)~~
~~[deleted]~~

...

Appendix 9.12 ~~Certificate by the Council (rule 9.58 (1)(a)) [deleted]~~

Appendix 9.13 ~~Statement by the Lloyd's actuary (rule IPRU(INS) 9.58 (1)(b)) [deleted]~~

Appendix 9.14 ~~Certificate by syndicate actuary (rule IPRU(INS) 9.58 (1) [deleted]~~

Appendix 9.15 ~~Auditor's report (rule IPRU (INS) 9.58(3)) [deleted]~~

Appendix 9.16 ~~Accounting classes (rule IPRU (INS) 9.49(1)(b)) [deleted]~~

Appendix 9.17 ~~Accounting records (rule IPRU (INS) 9.60(3)) [deleted]~~

Appendix 9.18 ~~Auditor's report (rule IPRU (INS) 9.60(7)) [deleted]~~

APPENDIX 9.1 (rules 9.12 and 9.13)

BALANCE SHEET AND PROFIT AND LOSS ACCOUNT

(FORMS 1 TO 3 AND 10 TO 19)

...

Statement of solvency – general insurance business

Name of insurer

Global business/UK branch business/EEA branch business

Financial year ended

Solo solvency calculation/~~Adjusted solo solvency calculation~~

...

Instructions for completion of Form 1

...

~~Instructions 6-12 only apply to firms that do not meet the conditions specified in *GENPRU 2.1.13R(2)*, i.e. that are not required to perform an adjusted solo calculation under *INSPRU 6.1*.~~

...

~~Instructions 13-20 only apply to firms that meet the conditions specified in *GENPRU 2.1.9 R(2)*, i.e. that perform the adjusted solo solvency calculation in accordance with *INSPRU 6.1*.~~

Instructions 13-20 are deleted in their entirety. The deleted text is not shown.

~~Instructions 21 onwards apply to all firms.~~

21 ...

Statement of solvency – long-term insurance business

Name of insurer

Global business/UK branch business/EEA branch business

Financial year ended

Solo solvency calculation/~~Adjusted solo solvency calculation~~

...

Instructions for completion of Form 2

...

~~Instructions 5-14 only apply to firms that do not meet the conditions specified in *GENPRU 2.1.13 R(2)*, i.e. that are not required to perform an adjusted solo calculation under *INSPRU 6.1*.~~

...

~~Instructions 15-23 only apply to firms that meet the conditions specified in *GENPRU 2.1.13R(2)*, i.e. that perform the adjusted solo solvency calculation in accordance with *INSPRU 6.1*.~~

Instructions 15-23 are deleted in their entirety. The deleted text is not shown.

~~Instructions 24 onwards apply to all firms.~~

24 ...

...

Instructions for completion of Form 3

...

~~Instructions 10-32 only apply to firms that do not meet the conditions specified in *GENPRU* 2.1.9R(2), i.e. that are not required to perform an adjusted solo calculation under *INSPRU* 6.1.~~

...

~~Instructions 33-57 only apply to firms that meet the conditions specified in *GENPRU* 2.1.13R(2), i.e. that perform the adjusted solo solvency calculation in accordance with *INSPRU* 6.1.~~

Instructions 33-57 are deleted in their entirety. The deleted text is not shown.

~~Instructions 58 onwards apply to all firms [deleted]~~

58 ...

Calculation of general insurance capital requirement – premiums amount and brought forward amount

Calculation of general insurance capital requirement– premiums amount and brought forward amount Form 11

Name of insurer
 Global business / UK branch business / EEA branch business
 Financial year ended
 General/long-term insurance business

	Company registration number	GL/UK/CM	day	Month	Year	units
R11						£000

...
 Excess (if any) over ~~£53.5M~~ 61.3M EURO
 ...

	This Financial Year	Previous Year
	1	2
33		

Calculation of general insurance capital requirement – claims amount and result

Calculation of general insurance capital requirement– claims amount and result

Form 12

Name of insurer

Global business / UK branch business / EEA branch business

Financial year ended

General/long-term insurance business

Company registration number GL/UK/CM

R12						
-----	--	--	--	--	--	--

...
 Excess (if any) over ~~£37.5M~~ 42.9M EURO x 0.03
 ...

	This Financial Year 1	Previous Year 2
33		

Instructions for completion of Form 16

...

- 1b Only transfers from or to the *general insurance business* technical account in respect of any equalisation provisions that are created as a result of a regulatory requirement are to be included at line 12.

...

APPENDIX 9.2 (rules 9.14 to ~~9.22~~ 9.21)

GENERAL INSURANCE BUSINESS: REVENUE ACCOUNT AND ADDITIONAL INFORMATION

(FORMS 20a AND 20 TO ~~39~~ 36)

...

Instructions for completion of Form 24

...

4. The amounts shown at lines 51 to 54 must exclude any equalisation provisions that are created as a result of a regulatory requirement.

...

...

Instructions for completion of Form 28

...

3. The amounts shown at lines 51 to 54 must exclude any equalisation provisions that are created as a result of a regulatory requirement.

...

Forms 37 to 39 are deleted in their entirety. The deleted text is not shown.

...

Appendix 9.7 is deleted in its entirety. The deleted text is not shown.

...

Appendix 9.9 is deleted in its entirety. The deleted text is not shown.

...

Appendices 9.12 to 9.18 are deleted in their entirety. The deleted text is not shown.

...

Annex M

**Amendments to the Interim Prudential sourcebook for Investment Businesses
(IPRU(INV))**

In this Annex, underlining indicates new text and striking through indicates deleted text.

4 Chapter 4: Lloyd's firms

4.1 Application

...

- 4.1.3 D The directions in *IPRU(INV)* 4.4.1D to ~~4.4.5D~~ and 4.5.1D are given to the *Council* and to the *Society* acting through the *Council*.

...

- 4.2.2 G The directions in *IPRU(INV)* 4.4.1D to ~~4.4.5D~~ and 4.5.1D are given under section 318 of the *Act* (Exercise of powers through Council), for the purpose of achieving the objective specified, as required by section 318(2) of the *Act*, in *IPRU(INV)* 4.3.1D.

- 4.2.3 G *Underwriting agents* are subject to regulation by the *Society* as well as by the *FSA*. In particular, they are subject to requirements as to their financial resources and as to making and maintaining accounting records, set by the *Society*. The *FSA* is satisfied that *underwriting agents* will be subject to adequate financial resource and accounting requirements as long as they remain subject to and comply with requirements at least equivalent to Lloyd's Capital and Solvency Requirements 2001 and the relevant parts of, or requirements made under Lloyd's Underwriting Agents Byelaw (No. 4 of 1984), in each case as amended and in force immediately before *commencement*. Accordingly, instead of imposing an obligation directly on *underwriting agents*, the directions in *IPRU(INV)* 4.4.1D to ~~4.4.5D~~ and 4.5.1D require the *Society* to require those firms to comply with the relevant requirements.

...

4.3 SPECIFICATION OF OBJECTIVE

- 4.3.1 D The directions in *IPRU(INV)* 4.4.1D to ~~4.4.5D~~ and 4.5.1D are given in relation to the exercise of the powers of the *Society* and of the *Council* generally, with a view to achieving the objective that *underwriting agents* have adequate financial resources to support, and keep and preserve adequate accounting records in respect of their business at Lloyd's.

...

- 4.4.2 D ~~The *Society* must give the *FSA* a report of each *underwriting agent's* compliance with the financial resource requirements referred to in *IPRU(INV)* 4.4.1D as at the end of each quarter (determined by reference to each *underwriting agent's accounting reference date*). [deleted]~~
- 4.4.3 D ~~The report referred to in *IPRU(INV)* 4.4.2D must reach the *FSA* within two months of the end of the relevant quarter and must state:~~
- ~~(1) whether the *Society* has any information indicating or tending to indicate that, during the quarter to which the report relates, the *underwriting agent* failed to meet the financial resource requirements referred to in *IPRU(INV)* 4.4.1D;~~
 - ~~(2) whether, at the end of the quarter to which the report relates, the *underwriting agent* failed to meet the financial resource requirements referred to in *IPRU(INV)* 4.4.1D; and~~
 - ~~(3) the nature and extent of any failure to comply reported under (1) or (2) and the actions taken or to be taken by the *Society* in response to this. [deleted]~~
- 4.4.4 D ~~In addition to the reports required under *IPRU(INV)* 4.4.2D, the *Society* must give the *FSA* an annual report on each *underwriting agent's* compliance or non-compliance with financial resource requirements as at the end of that *underwriting agent's* financial year. [deleted]~~
- 4.4.5 D ~~The report in *IPRU(INV)* 4.4.4D must reach the *FSA* within seven months of that *underwriting agent's* accounting reference date and must:~~
- ~~(1) confirm that:~~
 - ~~(a) the *Society* has received from that *underwriting agent* in respect of the financial year to which the report relates, all relevant attachments to the Annual Financial Return that the *underwriting agent* is required to make to the *Society* under the requirements identified in *IPRU(INV)* 4.4.1D;~~
 - ~~(b) that *underwriting agent* met the applicable financial resource requirements at the end of the financial year to which the report relates; and~~
 - ~~(c) the *Society* is not aware of any matters likely to be of material concern to the *FSA* relating to that *underwriting agent's* compliance with financial resource requirements during the year to which the report relates, or arising from the attachments referred to in (a); or~~
 - ~~(2) if the *Society* is unable to give any of the confirmations required under *IPRU(INV)* 4.4.5D (1)(a), (b) or (c), set out in each case the~~

reasons why it is unable to give that confirmation. [deleted]

4.4.5A D The *Society* must submit the reports in *IPRU(INV)* 4.4.2D to IPRU(INV) 4.4.5D in accordance with the *rules* in SUP 16.3 (General provision on reporting). [deleted]

...

Chapter 5: Financial Resources

...

TABLE 5.2.2(1) CALCULATION OF OWN FUNDS AND LIQUID CAPITAL

...

PART II

DETAILED REQUIREMENTS

...

5A Material insurance holdings (Item 8)

(a) ...

(b) An item falls into this provision for the purpose of (a) if it is:

... (i) ...

... (ii) subordinated debt or another item of capital that forms part of the tier two capital resources that falls into Article 16(3) of the First Non-Life Directive or, as applicable, Article 27(3) of the Consolidated Life Directive GENPRU 2 or, as the case may be, INSPRU 7, or is an item of basic own funds under SOLPRU 3.

...

Chapter 9: Financial resources requirements for an exempt CAD firm

...

APPENDIX 9(1) (INTERPRETATION)

...

material insurance holdings (a) ...

(b) An item falls into this provision for the purpose of (a) if it is:

(i) ...

- (ii) subordinated debt or another item of capital that forms part of the *tier two capital resources* that falls into ~~Article 16(3) of the *First Non-Life Directive* or, as applicable, Article 27(3) of the *Consolidated Life Directive*~~ GENPRU 2 or, as the case may be, INSPRU 7, or is an item of *basic own funds* under SOLPRU 3.

...

13 Chapter 13: Financial Resource Requirements for Personal Investment Firms

...

TABLE 13.5.4(2) PART I

This table forms part of *rule 13.5.4*

EXEMPT CAD FIRM

ASSETS	CALCULATION	TYPE OF ADJUSTMENT
...		
(13) All other assets	... Eligible capital instruments include ordinary share capital, cumulative preference shares, perpetual securities and long-term subordinated loans, that are eligible for insurance undertakings under PRU 2 <u>GENPRU 2</u> or, as the case may be, <u>INSPRU 7</u> , or is an item of <i>basic own funds</i> under <u>SOLPRU 3</u> .	An Illiquid Adjustment
...		

Annex N

Amendments to the Conduct of Business Sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

4 Communicating with clients, including financial promotions (COBS 4)

...

4.10 Systems and controls and approving and communicating financial promotions

- 4.10.1 G The *rules* in *SYSC 3*, ~~and~~ *SYSC 4* and *SOLPRU 9* require a *firm* that communicates with a *client* in relation to *designated investment business*, or *communicates* or *approves a financial promotion*, to put in place systems and controls or policies and procedures, or an effective internal control system, in order to comply with the *rules* in this chapter.

...

11 Dealing and managing

...

11.8 Recording telephone conversations and electronic communications

...

- 11.8.3 R This section does not apply to the following *firms* or *persons*:

...

- (3) ~~a non-directive insurer~~ an insurer that is not a UK Solvency II firm;

...

Annex O

Amendments to the Insurance: Conduct of Business sourcebook (ICOBS)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

1 Annex 1 Application (see ICOBS 1.1.2R)

...

Part 4: Guidance

...

4 Solvency II Directive non-life business ~~Non-Life Directives: effect on territorial scope~~

4.1 G The ~~Non-Life Directives'~~ Solvency II Directive's scope covers *insurers* authorised under ~~those Directives~~ that Directive conducting *general insurance business*.

...

4.3 G The ~~Directives specify~~ Directive specifies minimum information requirements and permits *EEA States* to adopt additional mandatory rules. (See ~~article 7 of the Second Non-Life Directive~~ articles 178 and 180 of the Solvency II Directive).

4.4 G If the *State of the risk* is an *EEA State*, the ~~Directives provide~~ Directive provides that the applicable information rules shall be determined by that state. Accordingly, if the *State of the risk* is the *United Kingdom*, the relevant *rules* in this sourcebook apply. Those *rules* do not apply if the *State of the risk* is another *EEA State*. The territorial scope of other *rules*, in particular the *financial promotion rules*, is not affected since the Directives explicitly permits *EEA States* to apply rules, including advertising rules, in the 'general good'. (See ~~articles 28 and 41 of the Third Non-Life Directive~~ article 180 of the Solvency II Directive.)

...

8.4 G The effect of the Directive on this sourcebook is subject to the 'insurance derogation', which is the only 'derogation' in the Directive that the *FSA* has adopted for this sourcebook. The derogation applies to an *insurer* that is authorised under, and carrying on an *electronic commerce activity* within, the scope of the ~~Insurance Directives~~ Solvency II Directive and permits *EEA States* to continue to apply their advertising rules in the 'general good'.

...

4 Information about the firm, its services and remuneration

...

4.2 Additional requirements for protection policies for insurance intermediaries and insurers

...

4.2.6 G *Insurers* cannot carry on an *insurance mediation activity* in respect of a third party's products unless they can show a natural fit or necessary connection between their insurance business and the third party's products (see the restriction of business in *INSPRU* 1.5.13R and *SOLPRU* 9.11).

...

Annex P

Amendments to the Supervision manual (SUP)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise indicated.

2 Information gathering by the FSA on its own initiative

2.1 Application and purpose

Application

2.1.1 R Subject to SUP 2.1.1AR and SUP 2.1.1BR the application of this chapter is the same as the application of *Principle 11* (Relations with regulators).

2.1.1A R SUP 2.3.5R(2) does not apply to UK Solvency II firms, the Society or managing agents in relation to suppliers under material outsourcing arrangements.

2.1.1B R SUP 2.3.7R to 2.3.10R do not apply to UK Solvency II firms, the Society or managing agents.

2.1.1C G SOLPRU 9.7 and the Solvency II Regulation set out the outsourcing rules which apply to UK Solvency II firms, the Society and managing agents.

...

2.3 Information gathering by the FSA on its own initiative: cooperation by firms

...

2.3.9A G Under sections 165(7) and 167(2) of the Act the FSA may:

(1) impose requirements to provide information or documents on a person who provides any service (including for instance under outsourcing arrangements) to a UK Solvency II firm, the Society or managing agents; and

(2) appoint a person to carry out an investigation of a person who provides services (including under outsourcing arrangements) to an insurer.

2.3.10 G The FSA will normally seek information from the firm in the first instance, but reserves the right to seek it from a supplier under a material outsourcing arrangement if the FSA considers it appropriate, or to resort, where appropriate, to its powers under the sections referred to in SUP 2.3.9AG.

...

Auditors**3.1 Application**

...

3.1.10 G Other relevant sections of the Handbook (see SUP 3.1.9G)

Friendly society IPRU(FSOC)*Insurer* (other than a UK Solvency II firm or a *friendly society*) IPRU(INS)*Investment management firm, personal investment firm, securities and futures firm* (other than BIPRU investment firms) IPRU(INV)*UCITS firm* (UPRU)UK Solvency II firm SOLPRU*Society of Lloyd's* and *Lloyd's managing agents* SOLPRU
~~IPRU(INS)~~

...

Insurance market direction on rules concerning auditors and actuaries

3.1.13 D ...

- (3) Regulations made by the Treasury under section 342(5) and section 343(5) of Part XXII of the *Act* apply only to *actuaries* appointed by a *managing agent* in respect of the *insurance business* of a *syndicate*, in relation to the ~~*long term insurance business*~~ of that *syndicate* matters specified in the table at SUP 4.1.3R(5).

...

3.1.15G G Section 317(2) of the *Act* (The core provisions) provides that references in an applied *core provision* to an *authorised person* are to be read as references to a *person* in the class to which the *insurance market direction* applies. The effect of this, and of the *insurance market direction* set out at SUP 3.1.13 D, is that Part XXII of the *Act* (Auditors and Actuaries), applies also to auditors and *actuaries* who are appointed to report on the underwriting business of *members*. Part XXII is modified in its application to *members* by paragraph (3) of SUP 3.1.13 D with the effect that the regulations made under sections 342(5) and 343(5) of the *Act* relating to communications by *actuaries* will only apply where the *actuary* is appointed in relation to the matters specified in the table at SUP 4.1.3R(5) ~~to evaluate the *long term insurance business* of the *syndicate*~~. The regulations made

under sections 342(5) and 343(5) in relation to communications by auditors will apply in relation to both *general insurance business* and *long-term insurance business*.

...

- 3.1.18 G ~~SUP 4.6 sets out rules the effect of which is to require a *managing agent* to appoint an *actuary* in respect of the *insurance business* of each *syndicate* which it manages. [deleted]~~

...

...

4 Actuaries

4.1 Application

...

- 4.1.2 G This chapter applies to *long-term insurers* (including *friendly societies*) and other *friendly societies* ~~and to the *Society of Lloyd's* and *managing agents* at Lloyd's~~. This chapter does not apply to *actuaries* advising the auditors of *long-term insurers* under IPRU(INNS) 9.35(1A) or IPRU(FSOC) 5.11(2A), as they are not appointed to act on behalf of the *firm*.

- 4.1.2A G This chapter applies to a *UK Solvency II firm*, the *Society* and *managing agents* with regard to the *with-profits actuary function*. A *UK Solvency II firm*, the *Society* and *managing agents* should also consider the requirements under SOLPRU 9.6 to provide for an *actuarial function* and this chapter also applies to the extent that an external *actuary* is appointed to perform tasks of the *actuarial function* of a *UK Solvency II firm*, the *Society* and *managing agents*.

- 4.1.3 R **Applicable sections**

(1)	Category of firm	(2) Applicable sections or rules
(1)	<p>A <i>long-term insurer</i>, other than:</p> <p>(a) a <i>registered friendly society</i> which is a <i>non-directive friendly society</i>;</p> <p>(b) an <i>incorporated friendly society</i> that is a <i>flat rate benefits business friendly society</i>; and</p> <p>(c) an <i>incoming EEA firm</i>; <u>and</u></p> <p>(d) a <i>UK Solvency II firm</i>.</p>	<p><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.3 and <i>SUP</i> 4.5</p>
(2)	<p>A <i>friendly society</i>, other than a <i>friendly society</i> within (1) or (5).</p>	<p><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.4 and <i>SUP</i> 4.5</p>
(3)	<p>A Lloyd's managing agent, in respect of each syndicate it manages [deleted]</p>	<p><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.5, <i>SUP</i> 4.6 [deleted]</p>
(4)	<p>The Society of Lloyd's [deleted]</p>	<p><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.5, <i>SUP</i> 4.6 [deleted]</p>
(5)	<p>A <i>UK Solvency II firm</i>, the <i>Society</i> and <i>managing agents</i> in respect of:</p> <p>(a) <u>the <i>with-profits actuary function</i></u>; or</p> <p>(b) <u>an external <i>actuary</i> appointed to perform tasks of the <i>actuarial function</i> of a <i>UK Solvency II firm</i> for the purpose of <i>SOLPRU</i> 9.6 (see <i>SUP</i> 4.3.1AR).</u></p>	<p><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.3 (except for <i>SUP</i> 4.3.1R(1)(a), <i>SUP</i> 4.3.13R, <i>SUP</i> 4.3.14R and <i>SUP</i> 4.3.15R) and <i>SUP</i> 4.5</p>

4.2 Purpose

...

4.2.2 G ...

- (3) ~~*managing agents* of Lloyd's *syndicates* employ or use an *actuary* of appropriate seniority and experience to evaluate the liabilities associated with *insurance business* carried on at Lloyd's.~~ ~~[deleted]~~

- 4.2.3 G The functions described by *SUP* 4.2.2G(1) are performed by one or more *actuaries* (or some other person in accordance with *SOLPRU* 9.6.1R) who are required to hold office continuously and must (except for an external *actuary* appointed by a *UK Solvency II firm*, the *Society* or *managing agents*) be *approved persons*. The principal duty of an *actuary* appointed to perform these functions is to advise the *firm* (see *SUP* 4.3.13R to *SUP* 4.3.18G for the rights and duties of such an *actuary*).
- ...
- 4.2.5 G *Actuaries* act as a valuable source of information to the *FSA* in carrying out its functions. For example, in determining whether a *firm* satisfies the *threshold conditions*, the *FSA* has regard to whether the *firm* has appointed an *actuary* (or some other person with responsibility for the actuarial *function* required by *SOLPRU* 9.6.1R) with sufficient experience in the areas of business to be conducted by the *firm* (*COND* 2.5.7G(11)).
- 4.2.6 G In making appointments under this chapter and in allocating duties to *actuaries*, *firms* are reminded of their obligation under *SYSC* 2.1.1R or *SOLPRU* 9.2.3R(2)(a) to maintain a clear and appropriate apportionment of significant responsibilities so that it is clear who has which of those responsibilities and that the business and affairs of the *firm* can be adequately monitored and controlled by the *directors*, relevant *senior managers* and *governing body* of the *firm*.

4.3 Appointment of actuaries

Appointment by firms

- ...
- 4.3.1A R A *UK Solvency II firm*, the *Society* and *managing agents* must appoint an external *actuary* if it does not have the internal capability to comply with *SOLPRU* 9.6.1R and articles [] of the *Solvency II Regulation*.
- ...

Appointment by the FSA

- 4.3.3 R If a *firm*, which is required to appoint one or more *actuaries* under *SUP* 4.3.1R or *SUP* 4.3.1AR, fails to do so within 28 days of a vacancy arising, the *FSA* may appoint one or more *actuaries* to perform any function corresponding to the *actuarial function* or the *with-profits actuary function* on the following terms:
- (1) the *actuary* to be remunerated by the *firm* on the basis agreed between the *actuary* and the *firm* or, in the absence of agreement, on a reasonable basis; and
 - (2) the *actuary* to hold office until he resigns or the *firm* appoints another *actuary*.

...

Disqualified actuaries

- 4.3.11 R *A firm must not appoint under SUP 4.3.1R, SUP 4.3.1AR or as an individual with responsibility for the actuarial function under SOLPRU 9.1.6R, an actuary who is disqualified by the FSA under section 345 of the Act (Disqualification) from acting as an actuary either for that firm or for a relevant class of firm.*

...

The actuarial function

- 4.3.14 G *IPRU(INS) 9.4R and IPRU(FSOC) 5.1R require firms to which this section applies to cause an investigation to be made at least yearly by the actuary or actuaries appointed to perform the actuarial function, and to report on the result of that investigation. INSPRU 1.3 requires realistic basis life firms to calculate the with-profits insurance component as part of their capital resources requirements. The firm is responsible for the methods and assumptions used to determine the liabilities attributable to its long-term insurance business. ~~The obligation on friendly societies to obtain a report from the 'appropriate actuary' under section 87 of the Friendly Societies Act 1992 applies to a friendly society which is to receive a transfer of engagements under section 86 (transfer of engagements to or by a friendly society). The 'appropriate actuary' in this context is the actuary appointed to perform the actuarial function, rather than the appropriate actuary under SUP 4.4 (Appropriate actuaries).~~*

- 4.3.14A G *The obligation on friendly societies to obtain a report from the 'appropriate actuary' under section 87 of the Friendly Societies Act 1992 applies to a friendly society which is to receive a transfer of engagements under section 86 (transfer of engagements to or by a friendly society). The 'appropriate actuary' in this context is the actuary appointed to perform the actuarial function rather than the appropriate actuary under SUP 4.4 (Appropriate actuaries). For a directive friendly society, the 'appropriate actuary' in this context is the person responsible for the actuarial function under SOLPRU 9.6.1R or, if that person is not a qualified actuary, an actuary appointed under SUP 4.3.1AR or SUP 4.3.1R(1)(b).*

...

The with-profits actuary function

...

- 4.3.16A R *An actuary appointed to perform the with-profits actuary function must:*

...

(2)

(2A) where the firm is a UK Solvency II firm, the Society or a managing agent, advise the firm's governing body as to whether the assumptions used to calculate the future discretionary benefits within the technical provisions under SOLPRU 2.4.7R are consistent with the firm's PPFM in respect of those classes of the firm's with-profits business;

...

...

4.5 Provisions applicable to all actuaries

...

Actuaries' statutory duty to report

4.5.7 G ...

(2) These regulations oblige *actuaries* to report certain matters to the *FSA*. Sections 342(3) and 343(3) of the *Act* provide that an *actuary* does not contravene any duty by giving information or expressing an opinion to the *FSA*, if he is acting in good faith and he reasonably believes that the information or opinion is relevant to any functions of the *FSA*. These provisions continue to have effect after the end of the actuary's term of appointment.

In relation to Lloyd's, an effect of the *insurance market direction* set out at SUP 3.1.13D is that sections 342(5) and 343(5) of the *Act* (Information given by auditor or actuary to the *FSA*) apply also to *actuaries* who are appointed in relation to the matters specified in the table at SUP 4.1.3R(5) to evaluate the long-term insurance business of a syndicate.

...

Rights and duties

...

4.5.14 G The standards, codes and guidance issued from time to time by the Institute of Actuaries, ~~and~~ the Faculty of Actuaries and the Board for Actuarial Standards are important sources of generally accepted actuarial practice.

SUP 4.6 is deleted in its entirety. The deleted text is not shown.

...

6.3 Applications for variation of permission

...

- 6.3.13 G The application for variation of *Part IV permission* will need to provide information about the *classes of contract of insurance* for which variation of *Part IV permission* is requested and also those *classes* qualifying to be carried on an ancillary or supplementary basis. For example, an *insurer* applying to vary its *permission* to include *class 10* (motor vehicle liability, other than carrier's liability) must satisfy the FSA that it will meet, and continue to meet, *threshold condition 2A* (Appointment of claims representatives). *Firms* should note that, although the *FSA* is able in principle to use its power to give *Part IV permission* for an applicant to carry on a *regulated activity* for which it did not originally apply, this is not possible under the ~~Insurance Directives~~ *Solvency II Directive*, which set out minimum information requirements for an application for *authorisation* including information on the specified investments the applicant proposes to deal in.

...

7 Individual requirements

...

7.3 Criteria for varying a firm's permission

...

- 7.3.2 G The *FSA* may seek to vary a *firm's Part IV permission* on its own initiative in certain situations, including the following:

...

- (5) If the *firm* is a *UK Solvency II firm* or the *Society*, by applying a *capital add-on* where there has been a *standard formula significant risk profile deviation*, an *internal model significant risk profile deviation*, or a *significant system of governance deviation* (see *SOLPRU 4.28*).

...

9 Individual guidance

...

9.3 Giving individual guidance to a firm on the FSA's own initiative

...

9.3.2 G The *FSA* may give individual *guidance* to a *firm* on its own initiative if it considers it appropriate to do so. For example:

...

(5) in relation to the maintenance of adequate financial resources, the *FSA* may give a *firm* (other than a *UK Solvency II firm*, the *Society* or *managing agents*) individual *guidance* on the amount or type of financial resources the *FSA* considers appropriate, for example *individual capital guidance* for *BIPRU firms* and *insurers*; further *guidance* on how and when the *FSA* may give *individual capital guidance* on financial resources is contained in the Prudential Standards part of the *Handbook*:

...

(b) for an *insurer* (other than a *UK Solvency II firm*): *GENPRU* 1.2 and *INSPRU* 7.1;

...

(d) For an *insurer* (other than a *UK Solvency II firm*): *INSPRU* 7

(6) In the case of a *UK Solvency II firm* or the *Society*, instead of giving *individual capital guidance* on the amount or type of financial resources, the *FSA* may apply a *capital add-on* where there has been a *standard formula significant risk profile deviation*, an *internal model significant risk profile deviation*, or a *significant system of governance deviation* (see *SOLPRU* 4.28 and *SOLPRU* 4.36).

...

11 **Controllers and close links**

...

11.8 **Changes in the circumstances of existing controllers**

11.8.1 R A *firm* must notify the *FSA* immediately it becomes aware of any of the following matters in respect of one or more of its *controllers*:

...

(4) if a *controller*, who is authorised in another *EEA State* as a *MIFID investment firm*, *BCD credit institution* or *UCITS management company* or under the ~~*Insurance Directives*~~ *Solvency II Directive* or the *Insurance Mediation Directive*, ceases to be so authorised (registered in the case of an *IMD insurance intermediary*).

...

13 Exercise of passport rights by UK firms (SUP 13)

13.1 Application and purpose

...

13.1.3 G This chapter does not apply to:

...

- (3) any insurance activity by way of provision of services which is provided by an *EEA firm* participating in a *community co-insurance operation* otherwise than as *leading insurer*; article 26.2 190(2) of the *Second Non-Life Solvency II Directive* provides that only the *leading insurer* in such an operation is required to complete any passporting formalities (see also article 11 of the *Regulated Activities Order*); or

...

...

13.2 Introduction

...

13.2.3 G In some circumstances, a *UK firm* that is carrying on business which is outside the scope of the *Single Market Directives* has a right under the *Treaty* to carry on that business. For example, for an *insurer* carrying on both direct insurance and *reinsurance* business, the authorisation of *reinsurance* business is not covered by the *Insurance Directives Solvency II Directive*. The *firm* may, however, have rights under the *Treaty* in respect of its *reinsurance* business. Such *UK firms* may wish to consult with the *FSA* on their particular circumstances (see *SUP 13.12.2G*).

13.3 Establishing a branch in another EEA State

...

The conditions for establishing a branch

13.3.2 G A *UK firm* other than a *UK pure reinsurer* cannot establish a *branch* in another *EEA State* for the first time under an *EEA right* unless the conditions in paragraphs 19(2), (4) and (5) of Part III of Schedule 3 to the *Act* are satisfied. It is an offence for a *UK firm* which is not an *authorised person* to contravene this prohibition (paragraph 21 of Part III of Schedule 3 to the *Act*). These conditions are that:

...

- (3)

- (a) if the *UK firm's EEA right* derives from the *Insurance Mediation Directive* ...
- (b) in any other case:
 - (i) the *Host State regulator* has notified the *UK firm* (or, where the *UK firm* is passporting under the *Insurance Directives Solvency II Directive*, the *FSA*) of the *applicable provisions* or, in the case of a *UK firm* passporting under *MiFID* or the *UCITS Directive*, that the *branch* may be established; or
 - (ii) two *months* have elapsed beginning with the date on which the *FSA* gave the *consent notice*.

...

13.3.3 G Where the *UK firm* is passporting under the *Insurance Directives Solvency II Directive* and the *Host State regulator* has notified the *FSA* of the *applicable provisions*, then under paragraph 19(9) of Part III of Schedule 3 to the *Act*, the *FSA* is required to inform the *firm* of these provisions.

13.3.3A G (1) *SUP 13.3.3G*, ~~does~~ *SUP 13.3.5* and *SUP 13.3.6* do not apply to *UK pure reinsurers* as they have automatic passport rights on the basis of their *Home State authorisation* under the *Reinsurance Solvency II Directive*.

- (2) Under section 3 of Part III of the *General Protocol*, *Home State regulators* have agreed to inform *Host State regulators* if a *pure reinsurer* for which the *Home State* is responsible carries on business through a *branch* in the *Host State*. Therefore *SUP 13.5.1AR* requires a *UK firm pure reinsurer* passporting under the *Reinsurance Solvency II Directive* to notify the *FSA* of certain information relating to the *branch*.

...

Issue of a consent notice to the Host State regulator

13.3.5 G ...

(2)

- (a) If the *UK firm's EEA right* derives from the *Insurance Directives Solvency II Directive*, the *FSA* will give the *Host State regulator* a *consent notice* within three *months* unless it has reason to ...

...

- (c) If the *FSA* has required a ~~financial~~ recovery plan of a *UK firm* of the kind mentioned in ~~paragraph 1 of article 38 of the~~

~~Consolidated Life Directive~~ or paragraph 1 of article 20a of ~~the First Non-Life Directive~~ article 138(2) of the Solvency II Directive or a finance scheme of the kind mentioned in article 139(2) of the Solvency II Directive, the FSA ~~will not~~ would not expect to give a *consent notice* for so long as it considers that *policyholders* are threatened within the meaning of those provisions.

...

13.3.6 G ...

(2) The *consent notice* will contain, among other matters, the *requisite details* or, if the *firm* is passporting under the ~~Insurance Directives~~ Solvency II Directive, the *relevant EEA details* (see SUP 13 Annex 1R) provided by the *UK firm* in its *notice of intention* (see SUP 13.5 (Notices of intention)).

(3) ...

...

13.4 Providing cross border services into another EEA State

...

The conditions for providing cross border services into another EEA State

13.4.2 G A *UK firm*, other than a *UK pure reinsurer*, cannot start providing *cross border services* into another *EEA State* under an *EEA right* unless it satisfies the conditions in paragraphs 20(1) of Part III of Schedule 3 to the *Act* and, if it derives its *EEA right* from the ~~Insurance Directives~~ Solvency II Directive, paragraph 20(4B) of Part III of Schedule 3 to the *Act*. It is an offence for a *UK firm* which is not an *authorised person* to breach this prohibition (paragraph 21 of Part III of Schedule 3 to the *Act*). The conditions are that:

...

(2) if the *UK firm* is passporting under the ~~Insurance Directives~~ Solvency II Directive, the *firm* has received written notice from the *FSA* as described in SUP 13.4.6G; or

...

...

13.4.2E G SUP 13.4.2G and SUP 13.4.4G do ~~does~~ not apply to *UK pure reinsurers* as they have automatic passport rights on the basis of their *Home State authorisation* under the ~~Reinsurance~~ Solvency II Directive. No notification is required from *UK pure reinsurers* in respect of this provision of *cross border services*.

...

Issuing a consent notice or notifying the Host State regulator

- 13.4.4 G (1) ...
- (2)
- (a) If the *UK firm's EEA right* derives from the *Insurance Directives Solvency II Directive*, paragraph 20(3A) of Part III of Schedule 3 to the *Act* requires the *FSA*, within one *month* of receiving the *notice of intention*, to ...
- (b) ...
- (c) If the *FSA* has required of a *UK firm* a ~~financial~~ recovery plan of the kind mentioned in ~~paragraph 1 of article 38 of the Consolidated Life Directive or paragraph 1 of article 20a of the First Non-Life Directive~~ article 138(2) of the *Solvency II Directive* or a finance scheme of the kind mentioned in article 139(2) of the *Solvency II Directive*, the *FSA* ~~will not~~ would not expect to give a *consent notice* for so long as it considers that *policyholders' rights* are threatened within the meaning of those provisions.

...

...

Applicable provisions for cross border services

- 13.4.6 G ...
- (2) If the *UK firm* other than a *other than a pure reinsurer* is passporting under the *Insurance Directives Solvency II Directive*, but is not a pure reinsurer, then the *Host State regulator* may notify the *FSA* if there are any applicable provisions. If so, the *FSA* will inform the *UK firm* of the *applicable provisions*.

...

...

13.5 Notices of intention

Specified contents: notice of intention to establish a branch

...

- 13.5.1A R A *UK pure reinsurer* establishing a *branch* in a particular *EEA state* for the first time under the *Reinsurance Solvency II Directive* must submit a notice in the form set out in *SUP 13 Annex 1R*. Whenever possible, this

notification must be made as soon as the information specified in that form is known by the *firm*.

- 13.5.1B G *SUP 13.5.1R* does not apply to *UK pure reinsurers* as they have automatic passport rights on the basis of their *Home State authorisation* under the *Reinsurance Solvency II Directive*.

Specified contents: notice of intention to provide cross border services

- 13.5.2 R A *UK firm* wishing to provide *cross border services* into a particular *EEA State* for the first time under an *EEA right* must submit a notice in the form set out in

(1) ...

(1A) *SUP 13 Annex 3R* if the *UK firm* is passporting under the *Insurance Directives Solvency II Directive*; or

...

- 13.5.2A G *SUP 13.5.2R* does not apply to *UK pure reinsurers* as they have automatic passport rights on the basis of their *Home State authorisation* under the *Reinsurance Solvency II Directive*.

...

Translations

- 13.5.6 G (1) A *UK firm* passporting under the *Banking Consolidation Directive*, or the *Insurance Directives* or the *Reinsurance Solvency II Directive* may have to submit the *requisite details* or relevant details in the language of the *Host State* as well as in English. For a *UK firm* (other than a *pure reinsurer*) passporting under the *Insurance Directives Solvency II Directive* this translated document will not include the relevant UK details. Further information is available from the Passport Notifications Unit.

(2) ...

(3) A *UK firm* (other than a *pure reinsurer*) passporting under the *Insurance Directives Solvency II Directive* should keep the *EEA* and *UK* relevant details separate as, if the application is approved, only the former will be sent to the *Host State regulator*.

...

13.6 Changes to branches

- 13.6.1 G Where a *UK firm* is exercising an *EEA right*, other than under the *Insurance Mediation Directive* (see *SUP 13.6.9AG*) or the *Reinsurance Directive* (see *SUP 13.6.9BR*), and has established a *branch* in another *EEA State*, any changes to the details of the *branch* are governed by the *EEA Passport*

Rights Regulations. ...

- 13.6.1A G Because the exercise of passporting rights by *pure reinsurers* is not covered by the *EEA Passport Rights Regulations*, *pure reinsurers* are not subject to the guidance in SUP 13.6. However, *pure reinsurers* are subject to SUP 13.6.9BR.
- 13.6.2 G *UK firms* should note that if a *branch* in another *EEA State* ceases to provide services, this may represent a change in *requisite details* or, if the *firm* is passporting under the ~~*Insurance Directives*~~ *Solvency II Directive*, the *relevant EEA details* or *relevant UK details*.
- 13.6.3 G *UK firms* should also note that changes to the details of *branches* may lead to changes to the *applicable provisions* to which the *UK firm* is subject. These changes should be communicated to the *UK firm* either by the *Host State regulator*, or, if the *firm* is passporting under ~~*Insurance Directives*~~ *the Solvency II Directive*, via the *FSA*.

...

Firms, other than *pure reinsurers*, passporting under the ~~*Insurance Directives*~~ *Solvency II Directive*

- 13.6.6 G If a *UK firm* has exercised an *EEA right* under the ~~*Insurance Directives*~~ *Solvency II Directive* and established a *branch* in another *EEA State*, regulation 13(1) states that the *UK firm* must not make a change in the *relevant EEA details* ...
- ...
- 13.6.8 G If a *UK firm* has exercised an *EEA right* under the ~~*Insurance Directives*~~ *Solvency II Directive* and established a *branch* in another *EEA State*, regulation 15(1) states that the *UK firm* cannot make a change in any of the *relevant UK details* unless the *UK firm* has given a notice to the *FSA* stating the details of the proposed change at least one *month* before the change is effected.
- 13.6.9 G Where a *UK firm* with *Part IV permission* to carry on both *long-term* and *general insurance business*, is passporting under the ~~*Insurance Directives*~~ *Solvency II Directive* and wishes to extend its *general insurance business* to include *long term insurance business* (or vice versa), it should complete a new *notice of intention* and not a change to details notice.

...

~~Firms~~ *Pure reinsurers* passporting under the ~~*Reinsurance*~~ *Solvency II Directive*

- 13.6.9B R A ~~*UK firm*~~ *UK pure reinsurer* exercising its *EEA right* under the ~~*Reinsurance*~~ *Solvency II Directive* to establish a *branch* in another *EEA State* must notify the *FSA* of any changes in the information specified in SUP 13 Annex 1R. Whenever possible, this notification must be made as

soon as the change in information is known by the *firm*.

Changes arising from circumstances beyond control of a UK firm

- 13.6.10 G (1) If the change arises from circumstances beyond the *UK firm's* control, the *UK firm*:
- (a) ...
- (b) may, if it is passporting under the *Insurance Directives Solvency II Directive*, make a change to its *relevant UK details* under regulation 15(1) ...

The process

...

- 13.6.14 G If a *UK firm* is passporting under the *Insurance Directives Solvency II Directive*, then regulation 13(7) states that the *FSA* may not refuse to consent to a change unless, having regard to the change the *FSA* has reason:

...

...

13.7 Changes to cross border services

- 13.7.1 G Where a *UK firm* is exercising an *EEA right* under the *UCITS Directive*, *MiFID* or the *Insurance Directives Solvency II Directive* and is providing *cross border services* into another *EEA State*, any changes to the details of the services are governed by the *EEA Passport Rights Regulations*. ...

- 13.7.1A G Because the exercise of passporting rights by pure reinsurers is not covered by the *EEA Passport Rights Regulations*, only SUP 13.7.12G of SUP 13.7 applies to pure reinsurers.

...

Firms, other than pure reinsurers, passporting under the ~~*Insurance Directives Solvency II Directive*~~

- 13.7.4 G If a *UK firm* has exercised an *EEA right* under the *Insurance Directives Solvency II Directive* and is providing *cross border services* into another *EEA State*, ...

...

- 13.7.10 G Where a *UK firm* with *Part IV permission* to carry on both *long-term* and *general insurance business* is passporting under the *Insurance Directives Solvency II Directive* and wishes to extend its *general insurance business* to include *long term insurance business* (or vice versa), it should complete a new *notice of intention* and not a change to details notice.

...

~~Firms~~ Pure reinsurers passporting under the ~~Reinsurance~~ Solvency II Directive

- 13.7.12 G A *UK firm, which is a pure reinsurer*, providing *cross border services* under the ~~Reinsurance~~ Solvency II Directive is not required to supply notification of, or a change to the details of, its *cross border services*.

13.8 Changes of details: provision of notices to the FSA

...

- 13.8.2 G *UK firms, other than pure reinsurers*, passporting under the *Banking Consolidation Directive* or the ~~Insurance Directives~~ Solvency II Directive may be required to submit the change to details notice in the language of the *Host State* as well as in English.

SUP 13 Annex 1 Passporting: Notification of intention to establish a branch in another EEA state

...

6 Consolidated Life Assurance Solvency II Directive (Life insurance)

Note to section 6²

If the firm is a pure reinsurer, it should not complete section 6 of this form, but should complete section 8 instead.

...

6.6 Please confirm you have attached the following. †

...
<p>iii. For each of the first three years following the establishment of the <i>branch</i>, estimates of the <i>firm's</i> margin of solvency and the margin of solvency required and the method of calculation</p> <p>(a) <u>future Solvency Capital Requirement, as well as the calculation method used to derive those estimates; and</u></p> <p>(b) <u>future Minimum Capital Requirement, as well as the calculation method used to derive those estimates.</u></p>	<p>Attached</p> <p>Attached</p> <p>Attached</p>	<p><input checked="" type="checkbox"/></p> <p><input type="checkbox"/></p> <p><input type="checkbox"/></p>
...		
<p>v. For each of the first three years following the establishment of the <i>branch</i>, the details described below with regards to the business carried on in the <i>EEA State</i> concerned:</p> <p>a) a statement setting out [on both optimistic and pessimistic bases,] detailed estimates of income and expenditure in respect of direct business, reinsurance acceptances and reinsurance cessions; and</p> <p>b) a statement of estimates relating to <u>of the financial resources intended to cover underwriting liabilities <i>technical provisions, the Minimum Capital</i></u></p>	<p>Attached</p> <p>Attached</p>	<p><input type="checkbox"/></p> <p><input type="checkbox"/></p>

² Please note that this change needs to be in the same format as the current Note to Question 6.1 i.e. in a grey box on the left hand side of this part of the form.

<p><u>Requirement and the Solvency Capital Requirement.</u></p>		
<p>...</p>		
<p>The technical bases that the actuary <u>appointed in accordance with SUP 4.3.1R employee</u> who is approved to perform the <u>actuarial function (CF12)</u> proposes to use for each class of business to be carried on in the <i>EEA State</i> concerned, including the bases needed for calculating premium rates and <u>technical provisions</u> mathematical reserves.</p>	<p>Attached</p>	<p><input type="checkbox"/></p>
<p>...</p>		

Section 7 ~~First, Second and Third Non-Life Insurance~~ Solvency II Directives (Non-life insurance)

Note to section 7³

If the firm is a pure reinsurer, it should not complete section 7 of this form, but should complete section 8 instead.

...

Note to question 7.3

...

iii. If the *firm* covers (or intends to cover) risks relating to **legal expenses insurance**, please state, in question 7.3, the option chosen from those described in ~~Article 3(2) of Directive 87/344/EEC of 22 June 1987 on the coordination of laws, regulations and administrative provisions relating to legal expenses insurance~~ Article 200(1) of the Solvency II Directive.

...

7.6 Please confirm you have attached the following. †

...
...
iv. For each of the first three years following the establishment of the <i>branch</i> , estimates of the firm's: margin of solvency and the margin of solvency required and the method of calculation	Attached	<input type="checkbox"/>
(a) <u>future Solvency Capital Requirement, as well as the calculation method used to derive those estimates; and</u>	Attached	<input type="checkbox"/>
(b) <u>future Minimum Capital Requirement, as well as the calculation method used to derive those estimates.</u>	Attached	<input type="checkbox"/>
v. For each of the first three years following the establishment of the <i>branch</i> , the details described below about the business carried on in the EEA State concerned:		
a) estimates relating to expenses of management (other than cost of	Attached	<input type="checkbox"/>

³ Please note that this change needs to be in the same format as the current Note to Question 6.1 i.e. in a grey box on the left hand side of this part of the form.

<p>installation) and, in particular, those relating to current general expenses and commissions;</p> <p>b) estimates relating to premiums or contributions (both gross and net of all reinsurance ceded) and to claims (after all reinsurance recoveries); and</p> <p>c) estimates relating to of the financial resources intended to cover <u>technical provisions, the <i>Minimum Capital Requirement</i> and the <i>Solvency Capital Requirement</i> underwriting liabilities.</u></p>	Attached	<input type="checkbox"/>
...		

8 Reinsurance Solvency II Directive (Reinsurance)**Note to section 8⁴**

Only pure reinsurers should complete this section of this form.

8.1 Please confirm the type(s) of reinsurance activity to be carried out by the branch under the ~~Reinsurance~~ *Solvency II Directive* by ticking one of the boxes below.

...

10. Declaration

...

I enclose the following sections (mark the appropriate section)

...	...
Section 6 – Consolidated Life Assurance <i>Solvency II Directive</i> (Life insurance)	...
Section 7 – First, Second and Third Non-Life <i>Solvency II Directives</i> (Non-life insurance)	...
Section 8 – Reinsurance <i>Solvency II Directive</i> (Reinsurance)	
...	

⁴ Note to Handbook Team – we are not sure where this note should appear in the form – perhaps it should be as in Section 6 (see Note to Question 6.1?)

**SUP 13 Annex 3 Passporting: ~~Consolidated Life Directive and Third Non-Life Directive~~
Solvency II Directive**

**~~CONSOLIDATED LIFE ASSURANCE DIRECTIVE and THIRD NON-LIFE
INSURANCE~~ SOLVENCY II DIRECTIVE**

...

Purpose of this form

You should complete this form if you are a *UK firm*, other than a *pure reinsurer*, that wishes to exercise a passport right to provide *cross border services* in another *EEA State* under the *Consolidated Life Assurance Directive* and/or the *Third Non-Life Insurance Solvency II Directive*.

UK pure reinsurers have automatic passport rights on the basis of their *Home State* authorisation under the *Solvency II Directive* and are, therefore, not required to complete this form.

....

Important information you should read before completing this form

A *UK firm* can only use this form if it is entitled to provide *cross border services* into another *EEA State* subject to the conditions of the *Consolidated Life Assurance and/or the Third Non-Life Insurance Directive Solvency II Directive* (see Schedule 3 of the Financial Services and Markets Act 2000 (FSMA)). ...

...

3 ~~Consolidated Life Assurance~~ Solvency II Directive (Life insurance)

...

4 ~~First, Second and Third Non-Life Directives~~ Solvency II Directive (Non-Life insurance)

...

Note to Question 4.2

- (3) If the *firm* covers (or intends to cover) risks relating to **legal expenses insurance**, please state in section 4.2 the option chosen from those described in ~~Article 3(2) of Directive 87/344/EEC of 22 June 1987 on the coordination of laws, regulations and administrative provisions relating to legal expenses insurance~~ article 200(1) of the *Solvency II Directive*.

...

5. Declaration

...

I enclose the following sections (mark the appropriate section)

...	...
Section 3 – Consolidated Life Assurance <u>Solvency II Directive (Life insurance)</u>	...
Section 4 – First, Second and Third Non-Life Directives <u>Solvency II Directive (Non-life insurance)</u>	...
...	

13A Qualifying for authorisation under the Act

13A.1 Application and purpose

Application

...

13A.1.3 G

- (1) Under the *Gibraltar Order* made under section 409 of the *Act*, a Gibraltar firm is treated as an *EEA firm* under Schedule 3 to the *Act* if it is:
- (a) authorised in Gibraltar under the *Solvency II Directive Insurance Directives*; or
 - (aA) ~~authorised in Gibraltar under the *Reinsurance Directive*; or~~
[deleted]
 - (b) ...

...

13A.2 EEA firms and Treaty firms

- 13A.2.1 G ... A *person* may be a *Treaty firm*, where, for example, it carries on business that includes *regulated activities*, the right to carry on which does not fall within the scope of the *Single Market Directive* under which it is entitled to exercise an *EEA right*, for example, *reinsurance* in the case of a direct insurer to which the ~~*Insurance Directives*~~ *Solvency II Directive* applies apply.

...

13A.3 Qualifications for authorisation under the Act

EEA firms

...

- 13A.3.1 G ~~A *pure reinsurer* with its head office in an *EEA State* that has not fully implemented the *Reinsurance Directive* may nevertheless be accepted as satisfying the conditions to be an *EEA pure reinsurer* if the *firm* provides satisfactory evidence that the prudential requirements of the *Reinsurance Directive* have been implemented by that *EEA State* and that they apply to the *firm*. The *firm* may then be deemed to be authorised under the *Reinsurance Directive* in that *EEA State*.~~ [deleted]

...

13A.3.1 G

1

- (1) An *EEA firm* that is carrying on both direct insurance and *reinsurance* business will be entitled to passport under Schedule 3 to the *Act* in relation to the direct *insurance business*. It will also have a *Treaty right* under Schedule 4 to the *Act* in relation to the *reinsurance* business if the *firm* has received *Home State authorisation* for the *regulated activity* of effecting and/or carrying out the relevant class of *insurance business* that includes *reinsurance* business for that class and the relevant provisions of the law of the *Home State* satisfy the conditions laid down by the *Insurance-Directives Solvency II Directive* relating to the carrying on of that activity (see *SUP* App 3.10.13G).
- (1A) An insurance company with its head office in an *EEA State* other than the *United Kingdom* that is carrying on pure *reinsurance* business in that State, and which has received authorisation ~~(or is deemed to be authorised)~~ under the *Reinsurance Solvency II Directive* from its *Home State* (an *EEA pure reinsurer*), has an automatic *EEA right* to passport into the *United Kingdom* by establishing a *branch* in the *United Kingdom* or by the provision of *cross border services*. ...
- (2) ~~An insurance company with its head office in an *EEA State* other than the *United Kingdom* that is carrying on pure *reinsurance* business in that State, and which wishes to carry on such business in the *United Kingdom* and is authorised by its *Home State* but not yet under the *Reinsurance Directive*, is advised to discuss its particular requirements with the Authorisation Department. It may be entitled to exercise a *Treaty right* provided it satisfies the conditions in paragraph 3(1) of Schedule 4 to the *Act* (see *SUP* 13A.3.4G). Otherwise, it will have to seek a *Part IV permission* (see the *FSA* website “How do I get authorised”: <http://www.fsa.gov.uk/Pages/Doing/how/index.shtml>).~~
[deleted]

...

13A.4 EEA firms establishing a branch in the United Kingdom

...

The notification procedure

- 13A.4.4 G (1) When the *FSA* receives a consent notice from the *EEA firm's Home State regulator*, it will, under paragraphs 13(2)(b), (c) and 13(3) of Part II of Schedule 3 to the *Act*, notify the *applicable provisions* (if any) to:
- (a) ...
- (b) in the case of an *EEA firm* passporting under the *Insurance Directives Solvency II Directive*, the *Home State regulator*; within two *months* of the notice date.

...

13A **Application of the Handbook to Incoming EEA Firms**
Annex
1

...

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
-------------------------------	--	---

...

SYSC	<p>SYSC 1 and SYSC 1 Annex 1 (Application of SYSC 2 and SYSC 3) contain application provisions only. SYSC 2 and SYSC 3 apply only to an <i>insurer</i>, <u>(other than a managing agent, and the Society and a Solvency II firm)</u>, as set out in SYSC 1 Annex 1.1.1R, which include the following exceptions:</p> <p>(1) SYSC 2.1.1R(1) and SYSC 2.1.2G do SYSC 2 does not apply;</p> <p>(2) SYSC 2.1.3R to SYSC 2.2.3G apply, but only in relation to allocation of the function in SYSC 2.1.3 R(2) and only in so far as responsibility for the matter in question is not reserved by an EU instrument to the firm's Home State regulator SYSC 3.1.1R to 3.1.5G, SYSC 3.2.1G to 3.2.5BG and SYSC 3.2.7G to 3.2.36R do not apply; and</p> <p>(3) <u>the remainder of SYSC 3 applies</u>, but only in so far as responsibility for the matter in question is not reserved by an EU instrument to the firm's Home State regulator.</p>	<p>SYSC 2 and SYSC 3 do not apply if the <i>firm</i> has <i>permission</i> only for <i>cross-border services</i> and does not carry on <i>regulated activities</i> in the <i>United Kingdom</i> (SYSC 1 Annex 1.1.1 R). SYSC 2 and SYSC 3 have limited application for activities which are not carried on from a UK establishment (see SYSC 1 Annex 1.1.1 R (2A)). Otherwise, see column (2).</p> <p>The <i>common platform requirements</i> in SYSC 4 - SYSC 10 apply as set out in SYSC 1 Annex 1.2.2R.</p> <p>SYSC 11 - SYSC 17 do not apply.</p> <p>SYSC 18 applies.</p> <p>SYSC 19A does not apply.</p>
------	--	---

...

FIT	<p>... <u>FIT applies in a limited way in relation to an incoming EEA firm that is a Solvency II undertaking (see FIT</u></p>	Does not apply.
-----	--	-----------------

1.2.4BG).

...

INSPRU does not apply unless the firm is an insurer to which *INSPRU* 1.5.33R applies. *INSPRU* does not apply.

U

...

13A Matters reserved to a Home State regulator

Annex

2

...

Requirements in the interest of the general good

2

- ...
- (1) the *Single Market Directives* expressly reserve responsibility for the prudential supervision of a *MiFID investment firm*, *BCD credit institution*, *UCITS management company* or passporting ~~*insurance undertaking*~~ *Solvency II undertaking* to the *Firm's Home State regulator*. The *Insurance Mediation Directive* reaches the same position without expressly referring to the concept of prudential supervision. Accordingly, the *FSA*, as *Host State regulator*, is entitled to regulate only the conduct of the firm's business within the *United Kingdom*;

...

Application of SYSC 2 and SYSC 3

4

SYSC 2 and *SYSC 3* only apply to an *insurer*, (other than a *managing agent*, and the *Society* and a *UK Solvency II firm*). See paragraph 8 below for a discussion of how the *common platform requirements* apply. *SYSC 2.1.1R* and *SYSC 2.1.2G* do not apply for a relevant *incoming Treaty firm*. The *FSA* ~~considers that it is entitled, in the interests of the general good, to impose the requirements in *SYSC 2.1.3R* to *SYSC 2.2.3G* (in relation to the allocation of the function in *SYSC 2.1.3R(2)*) and *SYSC 3* on an *incoming EEA firm* and apply to an *incoming Treaty firm*; but only in so far as they relate to those categories of matter responsibility for which is not reserved to the *firm's Home State regulator*. The requirements in *SYSC 3*, other than *SYSC 3.1.1R* to *SYSC 3.1.5G*, *SYSC 3.2.1G* to *3.2.5BG* and *SYSC 3.2.7G* to *3.2.36R*, apply to an *incoming EEA firm*; but only in so far as they relate to those categories of matter responsibility for which is not reserved to the *firm's Home State regulator*.~~

...

13 Examples of how SYSC 3 and/or the common platform provisions apply in practice.

- (1) The Prudential Standards part of the *Handbook* ~~(with the exception of INSPRU 1.5.33R on the payment of financial penalties and the Interim Prudential sourcebook (insurers) (IPRU(INS)) (rules 3.6 and 3.7))~~ do not apply to an *insurer* which is an *incoming EEA firm*. Similarly, SYSC 3 does not require such a *firm*:
- (a) ~~to establish systems and controls in relation to financial resources (SYSC 3.1.1R); or~~
 - (b) to establish systems and controls for compliance with that Prudential Standards part of the *Handbook* (SYSC 3.2.6R); ~~or~~
 - (c) ~~to make and retain records in relation to financial resources (SYSC 3.2.20R and SYSC 9.1.1R to 9.1.4G).~~

...

14 Incoming EEA firms changing details, and cancelling qualification for authorisation

14.1 Application and purpose

Application

...

- 14.1.3 G (1) Under the *Gibraltar Order* made under section 409 of the *Act*, a Gibraltar firm is treated as an *EEA firm* under Schedule 3 to the *Act* if it is:
- (a) authorised in Gibraltar under the ~~*Insurance Directives*~~ *Solvency II Directive*; or
 - (b) ...

...

14.2 Changes to branch details

...

Firms passporting under the ~~*Insurance Directives*~~ *Solvency II Directive*

- 14.2.5 G (1) Where an *incoming EEA firm*, passporting under the ~~*Insurance Directives*~~ *Solvency II Directive* has established a *branch* in the *United Kingdom*, ...
- (2) ...

...

14.3 Changes to cross border services

- 14.3.1 G Where an *incoming EEA firm* passporting under the *MiFID*, *UCITS Directive* or *Insurance Directives Solvency II Directive* is exercising an *EEA right* and is providing *cross border services* into the *United Kingdom*, the *EEA Passport Rights Regulations* govern any changes to the details of those services. ...

...

Firms passporting under the ~~Insurance Directives~~ Solvency II Directive

- 14.3.5 G If an *incoming EEA firm* passporting under the ~~Insurance Directives~~ Solvency II Directive is providing *cross border services* into the *United Kingdom*, it must not make a change to the details referred to in regulation 7(1) unless it has complied with the relevant provisions.

...

Transfers of business

...

18.2 Insurance business transfers

Purpose

...

- 18.2.2A G Under Principle 4, a firm must maintain adequate financial resources. The FSA will carefully consider the financial resources of the transferor and the transferee in an insurance business transfer both before and after the relevant transfer.

...

Consultation with other regulators

- 18.2.24 G The *guidance* set out in *SUP 18.2.25G* to *SUP 18.2.30G* derives from the requirements of the ~~Insurance Directives~~ Solvency II Directive and the associated agreements between *EEA regulators*. Schedule 12 of the *Act* implements some of these requirements.
- 18.2.25 G (1) If the transferee is (or will be) an *EEA firm* (authorised in its *Home State* to carry on *insurance business* under the ~~Insurance Directives~~ Solvency II Directive) or a *Swiss general insurance company*, then the *FSA* has to consult the transferee's *Home State regulator*, who has 3 months to respond. It will be necessary for the *FSA* to obtain from the transferee's *Home State regulator* a certificate confirming that the transferee will meet the *Home State's* solvency margin requirements (if any) after the transfer.

- (2) If the transferee is *authorised* in the *United Kingdom*, the *FSA* will need to certify that the transferee will meet its solvency margin requirements after the transfer. If the *FSA* has required of a *UK firm* a financial recovery plan of the kind mentioned in ~~paragraph 1 of article 38 of the Life Directive (2002/83/EC) or paragraph 1 of article 20a of the First Non-Life Directive~~, article 138(2), article 139(2) and article 142(1) of the Solvency II Directive, the *FSA* will not issue a certificate for so long as it considers that *policyholders'* rights are threatened within the meaning of paragraph 1.

...

18.3 Insurance business transfers outside the United Kingdom

Purpose

- 18.3.1 G Under section 115 of the *Act*, the *FSA* has the power to give a certificate confirming that a *firm* possesses any ~~required minimum margin~~ necessary margin of solvency, to facilitate an *insurance business* transfer to the *firm* under overseas legislation from a firm authorised in another *EEA State* or from a *Swiss general insurance company*. This section provides *guidance* on how the *FSA* would exercise this power and on related matters.

...

18.4 Friendly Society transfers and amalgamations

...

- 18.4.4 G For a transfer to another *friendly society*, if the conditions of 87(1) and 87(2) of the Friendly Societies Act 1992 are met a report is required from the *appropriate actuary* of the transferee to confirm that it will meet the ~~required minimum margin~~ necessary margin of solvency. Where the conditions of 87(1) and 87(3) are met the *FSA* may require a report from the *appropriate actuary* of the transferee to confirm that it will have an excess of assets over liabilities.

...

- 18.4.17 G Brief details should be given of the date of the last actuarial valuation and the position revealed (surplus/deficit, ~~required minimum margin~~ necessary margin of solvency and free assets) for each participant.

...

- 18.4.25 G The criteria that the *FSA* must use in determining whether to confirm a proposed amalgamation or transfer are set out in schedule 15 to the Friendly Societies Act 1992. These criteria include that:

...

- (3) for a transfer, the transferee possesses the ~~required minimum margin~~

necessary margin of solvency after taking the proposed transfer into account or, where it is not required to maintain a ~~required minimum margin~~ necessary margin of solvency, possesses an excess of assets over liabilities (for a transferee that is a *Swiss general insurance company* or an *EEA firm*, this is evidenced by a certificate from its *home state regulator*).

...

App 1 Prudential categories and sub-categories

...

App 1.2 Purpose

App 1.2.1 G The purpose of this appendix is to give *guidance* on the prudential categories and sub-categories of *firm* used in the ~~Interim~~ Prudential sourcebooks and the Supervision manual. The prudential categories are defined in the *Glossary*, and some of the sub-categories are defined there and some in the glossaries of the Interim Prudential sourcebooks.

...

SUP App 1.3 Prudential categories and sub-categories

App 1.3.1

App 1.3.1 G **Prudential categories and sub-categories used in the Prudential sourcebooks and the Supervision manual**

<i>Prudential categories</i> (Note 1)	Applicable prudential requirements (Note 2)	Prudential sub-categories
--	--	----------------------------------

...

<i>Friendly society</i>	<i>IPRU(FSOC) and SOLPRU</i>	<i>Directive friendly society</i> <i>Incorporated friendly society</i> <i>Non-directive friendly society</i> <i>Registered friendly society</i> <i>Flat rate benefits business friendly society</i>
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...

<i>Incoming EEA firm</i>	<i>GENPRU, BIPRU, INSPRU, SOLPRU and IPRU(BANK)</i>	<i>EEA bank</i>
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...

<i>Insurer*</i>	<i>IPRU(INS) or IPRU(FSOC), GENPRU, INSPRU, <u>SOLPRU</u> and MIPRU</i>	<i>Long term insurer General insurer <u>UK Solvency II firm</u> <u>Non Solvency I firm</u> Friendly society (see above)</i>
...		
<i>Society of Lloyd's*</i> [Delete asterisk]	<i>INSPRU and IPRU(INS) <u>SOLPRU</u></i>	
...		
<i>UK ISPV</i>	<i><u>SOLPRU</u></i>	
...		

...

App 1.4 Relevance of prudential categories

App 1.4.1 G Many, but not all, of the categories are used only in the Prudential Standards part of the *Handbook* and the Supervision manual. The prudential category of a *firm* will normally determine:

- (1) which module or modules of the Prudential Standards part of the *Handbook* is or are applicable to the *firm*;

...

...

App 2 Insurers: Regulatory intervention points and run-off plans

App 2.1 Application

App 2.1.1 R Subject to SUP App 2.1.4R, SUP App 2.1 to 2.15 apply to an *insurer*, unless it is:

- (1) a *Swiss general insurer*; or
- (2) an *EEA-deposit insurer*; or
- (3) an *incoming EEA firm*; or
- (4) an *incoming Treaty firm*.

...

App G SUP App 2.14A and 2.15 applies to an *insurer* carrying on *with-profits*

2.1.3 *business*, but SUP App 2.15 only applies if COBS 20.2.53R (Ceasing to effect new contracts of insurance in a with-profits fund) also applies.

App 2.1.4 R SUP App 2.4 to 2.7 and 2.11 do not apply to a UK Solvency II firm, the Society, managing agents or a non-EEA insurer.

App 2.1.5 G The rules for the Society and UK Solvency II firms in difficulty or in an irregular situation are in SOLPRU 6.

App 2.2 Interpretation

App 2.2.1 R For the purpose of *SUP App 2.1 to 2.14*:

(1) "capital resources":

...

(b) ~~in relation to a participating insurance undertaking, means P+T, where P and T have the meanings given by *INSPRU 6.1.45R(3)(a)* and (e) respectively, as calculated in accordance with *INSPRU 6.1.43R*; and [deleted]~~

(c) ~~in relation to any other firm, which is not a UK Solvency II firm, the Society or a managing agent, means the firm's capital resources as calculated in accordance with *GENPRU 2.2.17R*; and~~

(d) ~~in relation to a UK Solvency II firm and the Society, means the firm's eligible own funds.~~

(2) "guarantee fund":

...

(b) ~~in relation to a participating insurance undertaking, means the amount of capital resources which that firm must hold to comply with *INSPRU 6.1.45R(2)*; [deleted]~~

(c) ~~in relation to a firm other than a UK Solvency II firm, the Society or a managing agent which is not covered by (a) or (b), carrying on general insurance business, means the amount of capital resources which that firm must hold to comply with *GENPRU 2.2.34R*; and~~

(d) ~~in relation to a firm other than a UK Solvency II firm, the Society or a managing agent which is not covered by (a) or (b), carrying on long-term insurance business, means the amount of capital resources which that firm must hold to comply with *GENPRU 2.2.33R*;~~

...

App 2.2.2 G The calculation of each of the *base capital resources requirement*, the *long-term insurance capital requirement* and the *general insurance capital requirement* is set out in *GENPRU* 2.1. The calculation of each of the "guarantee fund" and "required margin of solvency" for *non-directive friendly societies* is set out in chapter 4 of *IPRU(FSOC)*. None of these expressions apply to UK Solvency II firms, the Society or managing agents.

App 2.3 Purpose

App 2.3.1 G ~~To fulfil its obligations under the *Insurance Directives*, and a~~ As part of the *FSA's* risk-based approach to supervision, there are certain times when the *FSA* needs to monitor a *firm* more closely than it normally would. This is so the *FSA* can fulfil its function of supervising *firms* properly and meet the regulatory objective of securing an appropriate degree of protection for *consumers*.

App 2.3.1A G The application of the rules in SUP App 2 depends, among other things, on whether firms are subject to the Solvency II Directive (See SUP App 2.1). The rules for the Society and UK Solvency II firms in difficulty or in an irregular situation are in SOLPRU 6. Equivalent rules for other firms are contained in this appendix. The guidance in SUP App 2.14A, however, is of general application. The rules and guidance in relation to run-off plans is also of general application, pending the development of delegated acts and technical implementing measures covering this area under the Solvency II Directive.

App 2.3.2 G The rules in SUP App 2.1 to 2.14 require a *firm* to submit reports and information to the *FSA* when:

- (1) a *firm*, other than a *UK Solvency II firm*, the *Society* or a *managing agent*, is failing to satisfy *threshold condition 4* (Adequate resources) (see *COND* 2.2), and its capital resources have fallen below its required margin of solvency, or its guarantee fund; or
- (2) the capital resources of a *firm*, other than a *UK Solvency II firm*, the *Society* or a *managing agent*, have fallen below its *capital resources requirement*; or

...

App 2.3.3 G The *FSA* may also ask a *firm*, other than a *UK Solvency II firm*, the *Society* or a *managing agent*, to submit reports and information to it when the *firm's* capital resources fall below the level advised in *individual capital guidance* given to the *firm*.

App 2.3.4 ~~In accordance with the *Insurance Directives*, a~~ A *firm*, other than a *UK Solvency II firm*, the *Society* or *managing agents* whose capital resources

have fallen below its required margin of solvency, or its guarantee fund, is required, by the *rule* set out in this appendix, to submit a *scheme of operations*, together with an explanation of how its capital resources will be adequately restored. ~~In order to secure an appropriate degree of protection for consumers, the FSA applies the rule in this appendix to firms to which the provisions of the Insurance Directives would not otherwise apply.~~

- App 2.3.5 G A *firm* (whether within or outside the scope of the *Solvency II Directive*) which is entering into run-off is required to submit a *scheme of operations*, including an explanation of how its *liabilities to policyholders* will be met in full. Where the capital resources of ~~such a~~ *firm other than a UK Solvency II firm, the Society or managing agents*, subsequently fall below its required margin of solvency, the *firm* is required to submit a plan for restoration. The rules for the Society and UK Solvency II firms in difficulty or in an irregular situation are in SOLPRU 6.
- App 2.3.6 G Following a change in *control*, or the grant or variation of *permission*, the reports submitted help the FSA to identify when a *firm* (whether within or outside the scope of the *Solvency II Directive*) departs from the *scheme of operations* submitted as part of the notification of a change in *control*, or an application for the grant or variation of *permission*, and on which basis such notification or application was approved.
- App 2.3.7 G *Principle 4* of the FSA's Principles for Businesses provides that *firm's* should hold adequate financial resources, while GENPRU 1.2.26R requires a *firm other than a UK Solvency II firm, the Society and managing agents* to maintain overall financial resources which are adequate to ensure that there is no significant risk that it cannot meet its liabilities as they fall due. In considering these requirements, a *firm* may decide to maintain capital resources above the level advised in *individual capital guidance* given by the FSA, or, if no *individual capital guidance* has been given, above its *capital resources requirement*. The amount of any such additional capital resources held is at the discretion of the *firm*. However, the extent to which a *firm* matches these additional capital resources to the volatility of its capital base, in conjunction with the strength of its systems and controls environment, is likely to affect the frequency with which it is subject to intervention under this appendix.
- App 2.3.8 G ~~In relation to a firm carrying on with-profits insurance business, action which it takes either to restore its capital resources to the levels set by the intervention points in this appendix, or to prevent its capital resources falling below those points, should be consistent with Principle 6 of the FSA's Principles for Businesses. Principle 6 requires a firm to pay due regard to the interests of its customers and treat them fairly. [deleted]~~

...

App 2.5 Capital resources below required margin of solvency

- App 2.5.1 R Unless SUP App 2.5.3R applies:

- (1) if a *firm's* capital resources are such that they no longer equal or exceed its required margin of solvency; or
- (2) if a *firm* no longer complies with *GENPRU 2.2.32R* and *GENPRU 2.2.28R*, ~~or *INSPRU 6.1.45R(1)(a)* and *INSPRU 6.1.45R(1)(b)*~~, as applicable;

it must, within 28 days of becoming aware of this event, submit to the *FSA* a plan for the restoration of a sound financial position, including:

...

- (4) an explanation of how, if at all, and by when:
 - (a) it expects its capital resources to be restored to the required margin of solvency; or
 - (b) as the case may be, it expects to comply with *GENPRU 2.2.32R* and *GENPRU 2.2.28R*, ~~or *INSPRU 6.1.45R(1)(a)* and *INSPRU 6.1.45R(1)(b)*~~, as applicable.

...

App
2.5.3

R If a *firm*:

...

- (4) ~~submit~~ submits a plan for restoration which:
 - (a) explains why the *firm's* capital resources have fallen below its required margin of solvency or, as the case may be, it no longer complies with *GENPRU 2.2.32R* or *GENPRU 2.2.28R*, ~~or *INSPRU 6.1.45R(1)(a)* and *INSPRU 6.1.45R(1)(b)*~~, as applicable; and
 - (b) demonstrates how, if at all, and by when, the *firm* will restore it or, as the case may be, resume compliance with *GENPRU 2.2.32R* and *GENPRU 2.2.28R*, ~~or *INSPRU 6.1.45R(1)(a)* and *INSPRU 6.1.45R(1)(b)*~~, as applicable.

...

App 2.7 Capital resources below the level of individual capital guidance

...

App
2.7.3

G ~~In relation to a *firm* carrying on with-profits insurance business, if it intends either (a) to remedy a fall in the level of capital resources advised in its individual capital guidance, or (b) to prevent a fall in the level advised in that guidance, for example, in either case, by taking management action to de-risk a with-profits fund or by reducing non-contractual benefits for~~

~~policyholders, it should explain to the FSA how such proposed actions are consistent with the firm's obligations under PRIN 2.1 Principle 6 (Customers' interests). [deleted]~~

- App 2.7.4 G If a firm's capital resources fall below the level advised in *individual capital guidance* given to the firm and, at the same time, any one or more of SUP App 2.4.1R, SUP App 2.5.1R, SUP App 2.5.3R or SUP App 2.6.1R applies, the firm should first comply with those rules. Those rules are concerned with circumstances where capital resources are likely to have fallen to levels much lower than the level advised in *individual capital guidance* and are, in some cases, requirements imposed by the *Insurance Directives*.

...

App 2.8 Ceasing to effect contracts of insurance

- App 2.8.1 R If a firm (whether within or outside the scope of the Solvency II Directive) decides to cease to effect new *contracts of insurance*, it must, within 28 days of that decision, submit a run-off plan to the FSA including:

...

...

- App 2.8.5 G ~~See SUP App 2.11.2G for guidance on the period that the scheme of operations should cover. The scheme of operations required by SUP App 2.8.1R, when a firm ceases to effect new contracts of insurance, should cover the run-off period until all liabilities to policyholders are met.~~

App 2.9 Under control of a new parent undertaking

- App 2.9.1 G A firm (whether within or outside the scope of the Solvency II Directive) that has notified the FSA of a new *parent undertaking* may be requested to submit a *scheme of operations* (~~see SUP 11.5.5G~~). A *scheme of operations* would be requested if the significance and circumstances of the change were considered to be sufficient to merit that level of scrutiny. This is normally only likely to be necessary when there has been an ultimate change in *control*, or when, as a result of the change in *control*, significant changes are proposed to the firm's *regulated activities*, business plan or strategy. ~~A firm which has submitted a scheme of operations under SUP 11.5.5G, is not required to submit a further scheme of operations under this appendix unless SUP App 2.4, SUP App 2.5 or SUP App 2.8 applies. SUP App 2.13 does, however, apply to such a firm.~~

App 2.10 Grant or variation of permission

- App 2.10.1 G The FSA ~~may~~ will ask a UK Solvency II firms, the Society, managing agents and non-EEA insurers seeking a grant or variation of *permission* to provide a *scheme of operations* as part of the application process (see article 18 of

the Solvency II Directive). It may make a similar request to other *firms* (see *SUP* 6.3.25G). ~~Such a firm~~ *Firms* which have submitted such a *scheme of operations* are is not required to submit a further *scheme of operations* under this appendix unless *SUP* App 2.4, *SUP* App 2.5 or *SUP* App 2.8 applies. *SUP* App 2.13 and *SUP* 6 Annex 4 do, however, apply to such a *firm*.

App 2.11 Submission of a scheme of operations or a plan for restoration

...

App 2.11.2 G The *schemes of operation* required when a *firm's* capital resources have fallen below its required margin of solvency or its guarantee fund (see *SUP* App 2.5.1R and *SUP* App 2.4.1R, respectively) should cover a period which is sufficient to demonstrate that the *firm's* capital resources will be adequately restored. Typically this would be a period of at least three years. However, if a *scheme of operations* has expired, but *SUP* App 2.4.1R or *SUP* App 2.5.1R continues to apply, the *firm* should submit a new *scheme of operations*. ~~The *scheme of operations* required by *SUP* App 2.8.1R, when a *firm* ceases to effect new contracts of insurance, should cover the run-off period until all liabilities to policyholders are met.~~

...

App 2.11.4 G ~~In relation to a *firm* which carries on *with profits insurance business* and which submits a plan, the *FSA* would expect an explanation of how any actions it plans to take to restore capital resources to the level of the guarantee fund, required margin of solvency or *capital resources requirement* are consistent with the *firm's* obligations under *Principle 6* (Customers' interests). [deleted]~~

App 2.12 Content of a scheme of operations

...

App 2.12.5 G In relation to *firms* covered by *SUP* App 2.1 to 2.14, *IPRU(FSOC)* 4.1 sets out the *rules* relating to capital resources for *non-directive friendly societies* and *GENPRU* 2.1; ~~and *GENPRU* 2.2 and *INSPRU* 6.1~~ set out the *rules* relating to capital resources for every other *firms* not subject to the Solvency II Directive. *SOLPRU* 3 to *SOLPRU* 5 set out the *rules* relating to capital resources for UK Solvency II firms and the Society. The capital resources which a *firm* is required to maintain vary according to whether the *firm* has its head office in the *United Kingdom* or overseas, and depending on the nature of the *insurance business* it carries on. The information which a *firm* is required to submit under *SUP* App 2.12.1R should reflect the nature and content of the *rules* relating to capital resources identified above. For example, in order to satisfy *SUP* App 2.12.1R, a *firm* with its head office outside the *United Kingdom* which is carrying on direct *insurance business* in the *United Kingdom* should submit separate information concerning its world-wide activities and its *UK* activities.

- App 2.12.6 G ~~To reflect its obligations under GENPRU 2.2.22G or IPRU(FSOC) 4.1(2) (as applicable), in~~ In order to comply with SUP App 2.12.1R, a firm which carries on both *long-term insurance business* and *general insurance business* should submit separate information for each type of *insurance business*.
- ...
- App 2.12.9 R A forecast statement of capital resources (under SUP App 2.12.1R(2)(c)) must include the forecast capital resources and the forecast required margin of solvency, or, as the case may be, *MCR* and *SCR* at the end of each *financial year* or part *financial year*.
- App 2.12.10 G UK Solvency II firms, the Society and managing agents should comply with any delegated acts or implementing technical standards which may be adopted under article 35(6) and (7) of the Solvency II Directive to the extent that they supersede the requirements in SUP App 2.12.
- App 2.13 Obligations on firms which have previously submitted a scheme of operations**
- App 2.13.1 R A firm which has submitted a *scheme of operations* to the FSA, whether required by SUP App 2.4, SUP App 2.5 or SUP App 2.8, or as part of an application under SUP 6.3 (see SUP 6.3.25G), or SUP 6.4 (see SUP 6 Annex 4), ~~or SUP 11.5 (see SUP 11.5.5G)~~, or an amended *scheme of operations*, must during the period covered by that *scheme of operations*:
- ...
- App 2.13.4 G The FSA considers that a significant departure referred to in SUP App 2.13.1R(3) includes:
- ...
- (7) any other transaction or circumstance which is likely to have a material effect upon available assets ~~(as defined in IPRU(INS) 11.1).~~

SUP App 2.14 is deleted in its entirety. The deleted text is not shown

App 2.14A Fairness issues for with-profit firms in difficulty or in an irregular situation

- App 2.14A.1 G SUP App 2.14A applies to a firm carrying on with-profits business.

App 2.14A.2 G Action which a *firm* takes either to restore its capital resources to the levels set by the intervention points in this appendix or in *SOLPRU 6*, or to prevent its capital resources falling below those points, should be consistent with *Principle 6* of the *FSA's Principles for Businesses*. *Principle 6* requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly.

App 2.14A.3 G If a *firm* intends either (a) to remedy a fall in capital resources, or (b) to prevent such a fall, for example, by taking management action to lessen the risk of a *with-profits fund* or by reducing non-contractual benefits for *policyholders*, it should explain to the *FSA* how such proposed actions are consistent with the *firm's* obligations under *PRIN 2.1 Principle 6* (*Customers' interests*).

App 2.14A.4 G Where a *firm* submits a plan for restoration under this appendix or complies with *SOLPRU 6*, the *FSA* would expect an explanation of how any actions it plans to take to restore its capital resources are consistent with the *firm's* obligations under *Principle 6* (*Customers' interests*).

App 2.15 Run-off plans for closed with-profits funds

...

Financial projections

App 2.15.8 G A *firm's firm*, other than a *UK Solvency II firm*, the *Society* and *managing agents* should include in its run-off plan ~~should include~~:

...

App 2.15.8A G Subject to *SUP App 2.15.8BG* a *UK Solvency II firm*, the *Society* and a *managing agent* should include in its run off plan:

- (1) a forecast summary revenue account for the *with-profits fund*, in accordance with *SUP App 2.12.7R*;
- (2) a forecast summary balance sheet and *eligible own funds* and *SCR* for the *with-profits fund*, in accordance with *SUP App 2.12.8R*; and
- (3) a forecast summary balance sheet and *eligible own funds* and *MCR* and *SCR* for the entire *firm*, in accordance with *SUP App 2.12.8R* and *SUP App 2.12.9R*;

in each case, for at least a three-year period, beginning on the date of closure.

App 2.15.8B G Delegated acts or implementing technical standards may be adopted under article 35(6) and (7) of the *Solvency II Directive* in relation, among other things, to run-off plans. In that event *UK Solvency II firms*, the *Society* and

managing agents should comply with those acts and standards to the extent that they supersede SUP App 2.15.8AG.

...

App 2.15.11 G ~~A firm's~~ The run-off plan of a firm to which INSPRU 7 applies should include:

...

SUP App 2.16 is deleted in its entirety. The deleted text is not shown.

...

App 3.6 Freedom to provide services

...

Place of supply

App 3.6.6 G ... The location of risks and commitments is found by reference to the rules set out in paragraph 6 of schedule 12 to the *Act*, which derive from ~~article 1 of the Consolidated Life Directive and article 2 of the Second Non-Life Directive~~ article 13(13) and (14) of the Solvency II Directive. ...

App 3.10 Mapping of ~~Insurance Directives~~ the Solvency II Directive to the Regulated Activities Order

Introduction

App 3.10.1 G The *guidance* in Table 3 describes in broad outline the relationship between:

- (1) the insurance-related *regulated activities* specified in the *Regulated Activities Order*; and
- (2) the activities within the scope of the *Insurance Directives* *Solvency II Directive*

App 3.10.2 G This is a guide only and should not be used as a substitute for legal advice in individual cases

...

**Table 3: ~~Insurance~~ Solvency II Part II Part III RAO
RAO**

Directive activities	Activities	Investments
1. Insurance Directive Non-life <u>insurance</u> activities		
1. Taking up and carrying on direct non-life insurance business	Article 10	Article 75
2. Classes 1 to 18 of direct non-life insurance business in Point A of the Annex I to the <u>First Solvency II Directive</u>		Corresponding paragraphs 1 to 18 of Schedule 1, Part I
2. Consolidated Life Directive <u>insurance</u> activities		
1. Taking up and carrying on direct life insurance business	Article 10	Article 75
2. Classes I to IX of direct life insurance business in the Annex + II to the <u>Consolidated Life Solvency II Directive</u>		Corresponding paragraphs I to IX of Schedule 1, Part II

Meaning of contract of insurance

- 3.10.3 G ... Such funeral plans (to the extent that they are insurance) are also excluded from the ~~Insurance Directives~~ Solvency II Directive. It covers some contracts which might not otherwise be viewed as insurance in the *United Kingdom* (for example, contracts of guarantee). These contracts are also governed by the ~~Insurance Directives~~ Solvency II Directive. ...

The ~~Insurance Directives~~ Solvency II Directive

- App 3.10.4 G Article 1 of the ~~First Non-Life Solvency II Directive~~ and article 2 of the ~~Consolidated Life Directive~~ provides that the ~~Directives Directive~~ "concern lays down rules concerning ... the taking up and pursuit, within the Community, of the self-employed activity activities of direct insurance and reinsurance". By contrast, article ~~Article~~ 10 of the *Regulated Activities Order* (Effecting and carrying out contracts of insurance) also covers reinsurance.
- App 3.10.5 G Articles ~~2, 3 and 4~~ of the ~~First Non-Life Directive~~ and ~~article 3~~ of the ~~Consolidated Life Directive~~ 3 to 12 of the Solvency II Directive set out certain exclusions by reference to:

...

App 3.10.6 G Some of the exclusions referred to in mirror exclusions in the *Regulated Activities Order*. So, the exclusion for breakdown insurance in article 2(3) 6 of the *First Non-Life Solvency II Directive* is matched by a slightly narrower exclusion in article 12 of the *Regulated Activities Order* (Breakdown insurance). The separate treatment of benefit-in-kind funeral plans under the *Regulated Activities Order* (see SUP App 3.10.4G) is matched by their exclusion on a slightly wider basis in article 3(5) 10 of the *Consolidated Life Solvency II Directive*. Other requirements from ~~these Directives~~ the Solvency II Directive are also excluded from regulation by the *Exemption Order*.

App 3.10.7 G Most of the exclusions under the Directives, however, are not excluded from being *regulated activities*. For example, ~~article 3 of the Consolidated Life Directive and article 3 of the Non-Life Directive~~ exclude certain mutual associations whose annual contribution income falls below a defined threshold. In the *United Kingdom*, these include certain smaller *friendly societies* commonly referred to as "*non-directive friendly societies*". The activities of such societies are regulated under the *Act*, on a "lighter basis" than the activities of other insurers.

Territorial scope of the Regulated Activities Order and the ~~Directives~~ Directive

App 3.10.8 G ... By contrast, under the ~~Directives~~ *Solvency II Directive*, the responsibility, as between *EEA States*, for regulating the conduct of passported insurance services is determined by reference to the location of the risk or commitment, as defined in ~~article 1 of the Consolidated Life Directive and article 2 of the Second Non-Life Directive~~ article 13(13) and (14) of the Solvency II Directive.

...

Position of EEA insurers carrying out both direct and reinsurance business

App 3.10.13 G ~~The Insurance Directives do not apply to the authorisation to carry on reinsurance. The Solvency II Directive applies separately to the authorisation of direct insurance and reinsurance. But, the Insurance Directives do not~~ It does not, though, prevent insurance undertakings authorised under those Directives the Directive from carrying out reinsurance as well as direct insurance business. Article 13(2) of the First Non-Life Directive and article 10(2) of the Consolidated Life Directive state Article 30(2) of the Solvency II Directive states that financial supervision of insurance undertakings (the same applies to reinsurance undertakings) "shall include verification, with respect to the insurance undertaking's entire business of the ... undertaking, of its state of solvency, of the establishment of technical provisions, of its and of the assets covering them and of the eligible own funds ...". On that basis, *an insurance undertaking* authorised in another *EEA State* which carries on a mixed direct insurance and *reinsurance* business, and is, therefore, subject to the requirements of the ~~Directives~~ *Solvency II Directive*, will generally be treated as satisfying the conditions laid down by an *EU* instrument relating to the carrying on of the

regulated activity of effecting or carrying out contracts of insurance. This is for the purpose of paragraph 3 of Schedule 4 to the *Act* (Exercise of treaty rights). The *insurance undertaking* will, therefore, generally be able to qualify for *permission* as a *Treaty firm* for its *reinsurance* business if it follows the procedure provided for by Schedule 4 (see *SUP 13A.3.4G* to *SUP 13A.3.11G* (Treaty Firms)). This will be in addition to the *insurance undertaking* being an *EEA firm* under Schedule 3 of the *Act* for its direct insurance business.

...

Annex Q

Amendments to the Regulated Covered Bonds sourcebook (RCB)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.1 Introduction to sourcebook

...

- 1.1.7 G An insurer (which is not a UK Solvency II firm, ~~non-directive friendly society, incoming EEA firm~~ or an ~~incoming Treaty firm~~) may benefit from increased counterparty limits under *INSPRU 2.1.22R(3)(b)*. An insurer which is a UK Solvency II firm is subject to the rules in SOLPRU which transpose the Solvency II Directive.

...

Annex R

Amendments to the Enforcement Guide (EG)

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 8 Variation and cancellation of permission on the FSA's own initiative and intervention against incoming firms

...

Exercising the power under section 47 to vary or cancel a firm's part IV permission in support of an overseas regulator: the FSA's policy

...

- 8.19 Relevant Community obligations which the FSA may need to consider include those under the Banking Consolidation Directive, the ~~Insurance Directives~~ Solvency II Directive, the Investment Services Directive/Markets in Financial Instruments Directive; and the Insurance Mediation Directive. Each of these Directives imposes general obligations on the relevant *EEA competent authority* to cooperate and collaborate closely in discharging their functions under the Directives.

...

- 19 **Non-FSMA Powers**

...

Financial Conglomerates and Other Financial Groups Regulations 2004

...

- 19.64 The FSA's power to vary a firm's *Part IV permission* under section 45 of the *Act* has been extended under these Regulations. The FSA is able to use this power where it is desirable to do so for the purpose of:

...

- acting in accordance with specified provisions of the ~~Insurance Groups Directive~~ Solvency II Directive.

...

Annex S

Amendments to the Perimeter Guidance Manual (PERG)

In this Annex, underlining indicates new text and striking through indicates deleted text.

2 Authorisation and regulated activities

...

2.4 Link between activities and the United Kingdom

- 2.4.7 G *Electronic commerce activities*, other than *insurance business* falling within the scope of the ~~*Insurance Directives*~~ *Solvency II Directive*, provided by an *incoming ECA provider* will not be *regulated activities* (see PERG 2.9.18G(2)).

...

2.8 Exclusions applicable to particular regulated activities

Effecting and carrying out contracts of insurance

- 2.8.3 G The following activities are excluded from both the *regulated activities* of *effecting and carrying out contracts of insurance*.
- (1) In specified circumstances, the activities of an *EEA firm* when participating in a Community co-insurance operation are excluded. A Community co-insurance operation is defined in the ~~*Community Co-insurance Directive*~~ *Solvency II Directive*.
 - (2) ...
 - (3) *Electronic commerce activities* provided by an *incoming ECA provider* where those activities are outside the scope of the ~~*Insurance Directives*~~ *Solvency II Directive* (see PERG 2.9.18G).

...

Agreeing

- 2.8.15 G ... The provision of *electronic commerce activities* by an *incoming ECA provider* is also excluded from the *regulated activity* of agreeing to carry on certain other *regulated activities* (see PERG 2.7.21G). But this is not the case where the agreement relates to the *regulated activity* of *effecting or carrying out contracts of insurance* falling under the ~~*Insurance Directives*~~ *Solvency II Directive* (see PERG 2.8.3G). ...

...

2.9 Regulated activities: exclusions applicable in certain circumstances

...

Incoming ECA providers

2.9.18 G ...

- (2) ... Where activities consist of *electronic commerce activities*, an *incoming ECA provider* will not require *authorisation* for such activities in the *United Kingdom*. This does not extend to the *regulated activity of effecting or carrying out contracts of insurance* falling under the *Solvency II Directive Insurance Directives* (see *PERG 2.8.3G*). ...

...

Annex 2G Regulated activities and the permission regime

...

Notes to Table 2

Note 1:

See *IPRU(INS) Annex 10.2 Part II* for the groups of *classes of general insurance business* from the Annex I to the ~~*First non-Life Directive*~~ *Solvency II Directive*.

...

5 Guidance on insurance mediation activities

...

5.3 Contracts of insurance

...

5.3.8 G ... The location of the risk or commitment may be determined by reference to the *EEA State* in which the risk is situated, defined in article ~~2(d)~~ 13(13) of the ~~Second Non-Life Directive (88/357/EEC)~~ *Solvency II Directive* or the *EEA State* of the commitment, defined in article ~~1(1)(g)~~ 13(14) of the ~~Consolidated Life Directive (2002/83/EC)~~ *Solvency II Directive*. ...

...

8 Financial promotion and related activities

...

8.12 Exemptions applying to all controlled activities

Incoming electronic commerce communications (article 20B)

...

8.12.38 G ... However, article 20B does not apply to the following communications:

...

(2) an invitation or inducement to enter into a *contract of insurance* where:

(a) it is made by an undertaking which has received official authorisation for direct insurance in line with ~~article 4 of the *Consolidated Life Directive* or article 6 of the *First Non-life Directive*~~ article 14 of the *Solvency II Directive*; and

(b) the insurance falls within the scope of ~~any of the *Insurance Directives*~~ the *Solvency II Directive*; or

...

...

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