

Supervisory Statement | SS7/15

Appendix 2.7

Solvency II: supervision of firms in difficulty or run-off

March 2015



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY



Prudential Regulation Authority
20 Moorgate
London EC2R 6DA

Prudential Regulation Authority, registered office: 8 Lothbury, London EC2R 7HH.
Registered in England and Wales No: 07854923



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1 Introduction

1.1 This supervisory statement is addressed to UK Solvency II firms and to the Society of Lloyd's. It sets out how the Prudential Regulation Authority (PRA) expects to deal with firms in the circumstances envisaged by Article 144 of the Solvency II Directive, where a firm does not meet the minimum capital requirement (MCR) and where either the PRA considers that the finance scheme it has submitted is manifestly inadequate or the firm fails to comply with the approved scheme within three months from the observation of non-compliance with the MCR.

1.2 It is also addressed to firms in run-off which may fall within the ambit of the transitional provision set out in Transitional Measures 2 in the Transitional Measures Part of the PRA Rulebook.

1.3 This statement should be read alongside all relevant European legislation as well as the Undertakings in Difficulty Part of the PRA Rulebook.

1.4 This statement expands on the PRA's general approach as set out in its insurance approach document.⁽¹⁾ By clearly and consistently explaining its expectations of firms in relation to the particular areas addressed, the PRA seeks to advance its statutory objectives of ensuring the safety and soundness of the firms it regulates, and contributing to securing an appropriate degree of protection for policyholders. The PRA has considered matters to which it is required to have regard, and it considers that this statement is compatible with the Regulatory Principles and relevant provisions of the Legislative and Regulatory Reform Act 2006. This statement is not expected to have any direct or indirect discriminatory impact under existing UK law.

1.5 This statement has been subject to public consultation⁽²⁾ and reflects the feedback that was received by the PRA.

2 Firms in breach of the minimum capital requirement

2.1 The PRA will take the same approach to firms which are failing to meet the MCR, whether they are still being run by their directors or whether an administrator or liquidator has been appointed.

2.2 The PRA expects those firms to act in a way which avoids significant systemic disruption, while protecting vital economic functions and which ensures that policyholders are appropriately protected. The interests of shareholders and creditors other than policyholders are therefore likely to be of lesser priority for the PRA in discharging its statutory functions. This approach is aligned with Solvency II, which has

as its main objective the protection of policyholders and requires the PRA to take all measures necessary to safeguard the interests of insured persons when insurers or reinsurers fail to meet MCR.

2.3 The PRA will be particularly concerned to ensure that:

- policyholders can maintain their insurance cover or obtain alternative insurance cover on reasonable terms where this is critical to them or their business;
- payments to them, which are essential for their living necessities, continue without disruption; and
- where this becomes necessary, the method for distributing assets amongst creditors (and shareholders) is fair to both those whose claims have arisen and those who may have claims in the future, given the increased risk that the firm will not have sufficient assets to pay all creditors in full.

2.4 The PRA will require a firm with no realistic prospect of prompt restoration of compliance with the MCR to bring its business to a close in as rapid and orderly manner as is consistent with the generality of policyholders' best interests. This may well take time and there are many circumstances in which a run-off strategy is in the best interests of policyholders (whether the firm is solvent or insolvent) and thus consistent with the main objective of Solvency II.

2.5 A firm in this position will not be permitted by the PRA to effect new contracts of insurance but the firm may be permitted to continue activities necessary to carry out existing contracts in a manner, and for so long as, the PRA considers necessary in order to afford an appropriate degree of protection to policyholders. Where a firm continues carrying out contracts of insurance as principal under the Financial Services and Markets Act 2000 (FSMA), the firm would continue to be authorised and retain a Part 4A permission for these limited purposes. The effect of this would be that the firm would also remain subject to PRA supervision, to the ongoing requirements of the PRA Rules which transpose Solvency II and to the Solvency II Regulations during this time. The same will be the case where an insolvency practitioner has been appointed. The PRA would expect such a person to conduct the firm's affairs in a way which is compatible with the main objective of Solvency II, as well as with their own statutory duties.

(1) *The Prudential Regulation Authority's approach to insurance supervision*, June 2014; www.bankofengland.co.uk/publications/Documents/praapproach/insuranceappr1406.pdf.

(2) *PRA Consultation Paper CP16/14*, 'Transposition of Solvency II: Part 3', August 2014; www.bankofengland.co.uk/pradocuments/publications/cp/2014/cp1614.pdf

2.6 The PRA will seek to exercise its powers under FSMA (and in particular, section 55M) in order to satisfy the requirements of Article 144 of the Solvency II Directive by imposing an assets requirement on a firm which is failing to meet the MCR and is unable to rectify this. The purpose of such a requirement will be to restrict the disposal by the firm of its assets but will generally permit the firm to pay the necessary costs of administering its business and to pay policyholder claims as appropriate. Any other transactions are likely to require the PRA's approval to ensure (among other things) that assets are disposed of for fair value. Where the firm is subject to insolvency proceedings then any asset requirement would permit the insolvency practitioner to realise the firm's assets and distribute them, where necessary to ensure compliance with legal requirements arising from the insolvency process and where consistent with the PRA's objectives.

3 Firms in run-off

3.1 The PRA expects firms in run-off, which consider that they meet the conditions set out in Transitional Measures 2, to inform the PRA of their assessment of their circumstances

sufficiently before 1 January 2016, such that the PRA can determine whether it is satisfied that the conditions are met. In particular, the PRA will expect firms to have a credible plan for transferring or extinguishing all their existing insurance liabilities within the timescales specified in Transitional Measures 2.1 (1 January 2019 or 1 January 2021, according to their circumstances). Firms should note that, in order for these provisions to apply, the firm must not be part of a group containing any other insurer or reinsurer which is not also in run-off.

3.2 The PRA will notify supervisory authorities in other Member States of those firms which it considers meet the transitional provisions.