

Insurance Update.

PRA developments

Key dates

There has been significant activity over the recent period and this is set to continue into 2015. Set out below is an overview of some key publications from the PRA and other relevant dates.

Date	Description
7 November 2014	PRA consultation on implementation (CP16/14) closed.
21 November 2014	PRA consultation on Solvency II: further measures for implementation opened (CP24/14).
24 November 2014	PRA consultation on the PRA Rulebook: Part 2 opened (CP25/14).
26 November 2014	PRA consultation on changes to the approved persons regime to extend its reach in relation to insurers opened (CP26/14).
23 January 2015	PRA consultation on the PRA Rulebook: Part 2 (CP25/14) closes to comments.
30 January 2015	PRA consultation on Solvency II: further measures for implementation (CP24/14) closes to comments.
2 February 2015	PRA consultation on changes to the approved persons regime (CP26/14) closes to comments.
February – March 2015	PRA to publish feedback, policy statement and final rules to transpose the Solvency II Directive.

PRA consultation on Solvency II: further measures for implementation (CP24/14)

The PRA has commenced consultation on proposed measures for implementation of Solvency II following the publication of CP24/14. [Click here](#) for link.

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This consultation paper (“**CP**”) follows CP16/14: Transposition of Solvency II: Part 3 which made proposals for the transposition of the Solvency II Directive into the Prudential Regulation Authority (“**PRA**”) Rulebook.

The CP consults on proposed rules to align the PRA Rulebook with the Solvency II Directive regarding the appointment of actuaries and schemes of operations. It also consults on two national specific templates and associated amendments to the Reporting Part of the PRA Rulebook (as consulted on in CP16/14) which are relevant to the Society of Lloyd’s.

In addition, five draft supervisory statements are provided including the following:

- > Regulatory reporting, internal model outputs;
- > ORSA and the ultimate time horizon (non-life firms);
- > Quality of capital instruments; and
- > Treatment of pension scheme risk.

In relation to defined benefit pension schemes, the PRA’s guidance highlights areas which firms need to consider when assessing the risks posed by the scheme to the firm for SCR purposes. It clarifies the PRA’s expectations where staff are outsourced to an intra-group services company as well as the capturing of risk posed to the firm even when obligations are not required to be recognised on the solo balance sheet under International Financial Reporting Standards.

The consultation period closes to comments on 30 January 2015. The PRA is required to transpose the Directive by Tuesday 31 March 2015 and the Solvency II regime will apply to all affected firms from 1 January 2016

PRA consultation on the PRA Rulebook: Part 2 (CP25/14)

The PRA has published CP25/14, which sets out proposals to redraft certain modules of the PRA Handbook. It is the second in a planned series of consultations aimed at reshaping Handbook material inherited from the Financial Services Authority (“**FSA**”) to create a Rulebook, containing only PRA rules. The PRA Rulebook will appear in a new online website in mid-2015 and, until then, will appear on the existing Handbook site in PDF form. [Click here](#) for link.

Detailed proposals for the presentation of the online Rulebook were outlined in Chapter 10 of CP8/13. [Click here](#) for link.

This CP seeks views on:

- > draft rules that will be incorporated into the PRA Rulebook covering status disclosure, controllers, close links, notifications and systems and controls;
- > four draft supervisory statements which include guidance setting out the PRA’s expectations of firms in relation to the aggregation of holdings for the purpose of the prudential assessment of controllers and the internal governance of firms; and

- > a statement of policy that sets out the PRA's approach to insurance business transfers.

The main changes will affect SUP 11, 16 and 18 and SYSC 4-9. Whilst these parts of the Handbook will be re-drafted, the CP does not signal significant changes in policy.

The consultation closes on Friday 23 January 2015.

PRA consultation on changes to the approved persons regime (CP26/14)

The PRA has also opened consultation on CP26/14. This CP follows on from CP16/14, and sets out some further proposed changes to the PRA's rules to implement the 'fit and proper' requirement provisions of the Solvency II Directive, and to introduce a new Senior Insurance Managers Regime (SIMR). [Click here](#) for a link to CP26/14:

[Click here](#) for our analysis of the new regime and the implication for insurers.

These proposed rules, along with the expectations set out in some draft supervisory statements, will contain the regulatory framework to ensure that those individuals who run insurers have clearly defined responsibilities and behave with integrity, honesty and skill.

The CP sets out the PRA's proposals in relation to the:

- > scope of the PRA's proposed new SIMR for insurers;
- > allocation of responsibilities to senior insurance managers;
- > application of conduct standards to individuals performing key functions; and
- > assessment of fitness and propriety of those individuals.

It should be noted that the SIMR for insurers will reflect the particularities of insurers' business models and the relevant legislation, and will not be the same as the Senior Managers Regime (SMR) that was proposed for banks in CP14/14.

The PRA expects to publish further consultation material on the role of NEDs in the SIMR in early 2015, taking into account the context of both the insurance and banking regimes.

The consultation closes to comments on 2 February 2015.

PRA With-Profits Rules

Since legal cut-over, each of the PRA and FCA has designated rules and guidance within the existing FSA Handbook – some COBS 20 provisions were PRA designated. The PRA now intends to create the PRA Rulebook and hence all existing PRA designated COBS 20 provisions will be replaced with new prudential rules. CP 22/14 consults on the proposed new rules and a draft PRA supervisory statement on with-profits. [Click here](#) for a link to CP22/14.

The PRA's consultation will result in fewer rules applicable to with-profits businesses than at present. The intention is to provide a clearer focus and greater clarity between the roles of the PRA and FCA, which will continue to be supported by the framework set out in the With-Profits Memorandum of Understanding.

The new CP will also need to be read together with the proposed rules on the calculation of surplus funds, which are included in CP 16/14 and relevant to Solvency II firms. It is expected that the new rules will come into force at the same time as Solvency II, from 1 January 2016. UK Solvency II firms will also need to apply the rules in COBS 20 from the FCA (discussed below).

What are the new rules?

- > **Adequacy of assets:** Firms will be required to hold, within each of its with-profits funds, assets that are sufficient to meet with-profits liabilities (as defined);
- > **Distribution strategies:** With-profit firms will need to ensure that their distribution strategies are affordable, sustainable and are not expected to have a significant negative impact on the firm as a whole or the security of policyholders generally;
- > **With-profits support arrangements:** Firms will be required to adequately document the structure and terms and conditions of any with-profits support arrangements (including identifying the extent of any restrictions that apply to the use of those arrangements); and
- > **Definitions:** In addition to the above new rules, various key definitions relating to with-profits have been redrafted and are contained in the CP including definitions of "With-Profits Fund" and "With-Profits Policy Liabilities"

What does the draft supervisory statement cover?

- > **Solvency II ring-fenced fund regimes:** PRA expects that the Solvency II regulations determining "own funds" and the SCR capital requirement arising in respect of a RFF will be applied to each with-profits fund. Where a firm operates sub-funds within a With-Profits fund each one will need to be assessed under the rules for RFFs.
- > **Support arrangements:** Where support arrangements are exclusively for a with-profits fund, the PRA expects that they will fall within the with-profits fund RFF. Where support assets are not exclusively for the use of a with-profits fund, whether a firm can use those as part of its financial resources available to meet the liabilities of the with-profits fund will depend on a number of factors, including the financial strength of the overall firm. The PRA could expect a firm to regard that arrangement as being exclusive, in which case it may be in the RFF.
- > **Distribution strategies:** PRA does not expect firms to make distributions which could endanger security including when setting with-profits distribution strategies which accelerate the transfer of profits

outside the fund and particularly when considering special or one-off distributions.

- > **Significant changes in With-Profits funds:** PRA expects early information in relation to any plans to change the operation, management or business strategy of a with-profits fund (including closing to new business, changing run-off plans, reattribution or Part VII transfer).

FCA developments

FCA with-profits rules

The FSA issued two consultation papers on Solvency II transposition in 2011/2012, namely: Part 1: CP11/22 in November 2011 and Part 2: CP12/13 in July 2012. The second of these consulted on changes to with-profits rules and linked business (COBS 20 and 21).

The key driver behind the FSA consultation was the fact that the Solvency II concept of a ring-fenced run (“**RFF**”) was intended to operate on with-profits funds. Long-term funds more generally (including linked funds operated in NPFs) were not intended to be treated as RFFs. However, Solvency II does not contain rules that establish RFFs, it merely contains rules that operate on RFFs as established by national law. Hence, the FSA needed to create national laws that made with-profits funds RFFs and didn't result in other parts of long term funds being RFFs.

The solution was to:

- > articulate, for the first time, the specific inputs and outputs that determine the composition of a with profits fund;
- > remove the concept of a long term fund (and the associated internal contagion rules); and
- > apply the internal contagion rules to the with profits fund only, so that it is ring-fenced under national law and therefore a RFF for Solvency II purposes.

Note also that in the background there was ongoing tension over whether COBS 20 truly was a set of conduct rules (rather than prudential rules) and how COBS 20, and competence for with-profits more generally, would be divided between the FCA and PRA. The PRA rules are described above.

In FS14/1, the FCA proposes the following rules:

- > internal contagion rules, along the lines of the current INSPRU 1.5 requirements, such as separate identification of/accounting for with-profit fund assets, maintenance of with-profit fund assets to cover best estimate component of with-profit TPs, exclusive use of with-profit fund assets for with-profit business, no transfers out except for surplus established by actuarial investigation, etc; and
- > external support arrangements must be clearly documented in the firm's records and clearly and unambiguously set out in the PPFM.

[Click here](#) for a link to FS 14/1

Key dates

The PRA is required to transpose the Directive by Tuesday 31 March 2015, and the first tranche of rules needed to ensure that there is an operationally effective regime that will enable Solvency II implementation on 1 January 2016 will be commenced from that date.

The following sets out an overview of certain key dates over the past few months and into 2015 in relation to the EIOPA process.

Date	Description
10 October 2014	EC adopted the Delegated Acts and published them on its website.
31 October 2014	EIOPA submitted first set of ITS to the EC (covering approval processes, such as model approval and own fund approvals). The EC has three months (extendable by a further month) to endorse or reject/partially reject/amend).
2 December 2014	EIOPA public consultation on second set of Solvency II standards and guidelines opened (see below).
3 December 2014	EIOPA published the outcome of the public consultation related to the first set of the draft Guidelines for Solvency II (see below).
December 2014 to March 2015	EIOPA to consult on second set of ITS and Guidelines (covering qualitative requirements and supervisory transparency).
10 January 2015	End of three month objection period in relation to Delegated Acts. The Parliament or Council may either object to the Delegated Acts or extend the objection period by a further three months. If they do nothing, the Delegated Acts will enter into force on this date.
31 January 2015	End of three month EC review period in relation to the first set of the ITS. The EC may endorse or reject/partially reject/amend or extend the period by a further month.
February 2015	EIOPA to publish first set of Guidelines (covering approval processes).
2 March 2015	EIOPA public consultation on second set of Solvency II standards and guidelines closes to comments.
31 March 2015	Deadline for member states to have transposed the Solvency II Directive (as amended by the Omnibus II Directive) into national law.

Date	Description
1 April 2015	Approval processes formally commence, including internal model approvals.

FCA publishes findings of annuities review

The FCA has published TR14/20 which presents the findings of its thematic review of the non-advised sales practices of pension providers offering annuities to existing customers.

[Click here](#) for a link to TR14/20

The first thematic review into annuities carried out by the FCA (TR14/2) reported that many consumers were buying an annuity from their current pension provider, and that they may be missing out on a higher income in retirement as a result. The FCA found that some parts of the market were not working well for some consumers and specifically that many consumers do not shop around and switch provider, even when a high proportion of these would be better off doing so.

As a result, they announced a review that aimed at uncovering whether firms' sales and customer retention practices contributed to customers not shopping around and switching. The review considers the non-advised sales practices of pension providers offering annuities to their existing customers. The sample of firms covered 70% of this market, looking at material relating to the period September 2013 to November 2013.

The FCA found evidence indicating that firms' sales practices are contributing to consumers not shopping around and switching. At times, consumers are potentially buying the wrong type of annuity, in particular not purchasing an enhanced annuity when they may be eligible for one. As a result, consumers may be missing out on a potentially higher income in retirement.

As a result, the FCA is asking some firms to do further work to determine if their findings in relation to enhanced annuities are indicative of a more widespread problem and/or have led to poor consumer outcomes when buying annuities.

EIOPA launches public consultation on second set of Solvency II standards and guidelines

EIOPA has issued its consultation documents on the second set of Guidelines and Implementing Technical Standards for Solvency II. Comments are due by 2 March 2015, using the template provided on EIOPA's website. Comments on the "Call for Advice on recovery plan, finance scheme and supervisory powers in deteriorating financial conditions" are due by 18 February.

[Click here](#) for a link to the EIOPA web page.

Papers are being consulted on in respect of all three Pillars, including the following:

- > Pillar 1
 - Guidelines on the valuation of assets and liabilities;
 - Guidelines on the implementation of the long term guarantee measures
 - Implementing Technical Standard on the equity charge transitional.
- > Pillar 2
 - Guidelines on the extension of the recovery period;
 - Implementing Technical Standard on procedures when assessing external credit assessments;
 - Implementing Technical Standard on capital add-on.
- > Pillar 3
 - Guidelines on methods to determine the market share for the purpose of exemptions to supervisory reporting;
 - Guidelines on reporting and disclosure;
 - Guidelines on exchange of information on a systematic basis within colleges;
 - Implementing Technical Standard on procedures, formats and templates of the Solvency and Financial Condition Report.

Other areas, EIOPA is consulting on include Guidelines on the supervision of third country branches.

EIOPA final statement on the outcome of the public consultation related to the first set of the draft Guidelines for Solvency II

On 3 December, EIOPA published the final reports on the public consultation related to the first set of draft Guidelines for Solvency II. They complement the first set of Implementing Technical Standards and cover: own funds, standard formula SCR, technical provisions, group solvency, internal models, ORSA and governance, supervisory review process and equivalence. [Click here](#) for a link to the EIOPA website.

The Guidelines are to be issued in the first quarter of 2015.

In relation to “*Guidelines on classification of own funds*”, there are two key points to note:

- > **Dividend pushers and stoppers:** EIOPA notes that capital instruments should not contain dividend pushers and stoppers. We would note that the PRA continues to express the view that interest pushers are permitted in Tier 2 instruments that contain optional interest deferral where the pusher only acts to remove that option to defer. This is on the basis that the provisions requiring mandatory deferral of interest on breach of SCR “trump” both the compulsory payment and optional deferral provisions; and

- > **Fixed to floating rate instruments:** EIOPA has confirmed that moving from a fixed to a floating rate is not in all cases an unlimited incentive to redeem. This is relevant to any issuers that have included a fixed-to-floating rate feature in a perpetual instrument which otherwise fully meets the Solvency II Tier 2 rules in order to try to grandfather the instrument as Tier 1. If that was the only non-compliant feature then they may not get the bonus of Tier 1 grandfathering treatment and will instead only get Tier 2 treatment on a fully compliant basis.

PRIIPS Regulation – published in the Official Journal

The PRIIPS Regulation has been published in the Official Journal. The Regulation lays down uniform rules on the format and content of the key information document (“**KID**”) to be drawn up by 'packaged retail and insurance-based investment product' (“**PRIP**”) manufacturers and on the provision of the key information document to retail investors in order to enable retail investors to understand and compare the key features and risks of the PRIP. [Click here](#) for a link to the PRIIPS Regulation.

Key provisions include:

- > **Product intervention powers**

EIOPA will have the power to temporarily prohibit or restrict in the EU (i) the marketing, distribution or sale of certain insurance-based investment products, or (ii) a type of financial activity or practice of an insurance or reinsurance undertaking. Action adopted by EIOPA shall prevail over any previous action taken by a competent authority. The European Commission shall adopt delegated acts specifying criteria and factors to be taken into account by EIOPA.

- > **Sanctions**

Competent authorities will have the power to impose, in accordance with national law, at least the following administrative sanctions and measures:

- an order prohibiting the marketing of a PRIP;
- an order suspending the marketing of a PRIP;
- a public warning which indicates the person responsible for, and the nature of, the infringement;
- an order prohibiting the provision of a key information document which does not comply with specific requirements and requiring the publication of a new version of a key information document; and
- administrative fines.

> **Entry into force**

The Regulation comes into force on 29 December 2014 and it will apply directly in all Member States from 31 December 2016. By 31 December 2018, the Commission is expected to review the Regulation.

Indian insurance reforms may be delayed beyond the end of 2014

The Modi government's proposed reforms to the Indian insurance law are still the subject of close scrutiny by the select committee of the Rajya Sabha (the upper house of the Parliament of India). The reforms, first proposed as part of the Insurance Laws (Amendment) Bill (the "**Amendment Bill**") this Summer, include proposals to permit an increase of foreign investment in the insurance sector to 49% and potential changes to the concept of "Indian management and control".

The general thrust of the proposals contained in the Amendment Bill is to open up the Indian insurance sector to greater foreign investment, primarily by allowing foreign portfolio investors to hold shares in insurance companies within an overall cap of 49%. The Amendment Bill also leaves the definition of "Indian management and control" in relation to insurance companies as a matter to be determined by way of rules made by the Insurance Regulatory and Development Authority, suggesting that there may be cause to monitor this area carefully over the medium term.

However, the Modi government's attempts to build a cross-party consensus around the bill have been frustrated by calls from the main opposition parties for greater scrutiny through the committee process. The Amendment Bill is currently with the select committee of the Rajya Sabha which has been engaged in extensive discussions about the proposals with a number of stakeholders (including representatives from insurance companies, shareholders, banks and advisors). The committee was supposed to have submitted its report on the Amendment Bill to the Rajya Sabha by the end of November, although it has requested an extension of this deadline to sometime in early December. Consequently, passage of the Amendment Bill into law is likely to be delayed further still, with every chance that it may not be passed before the end of the Parliament's winter session on 23 December 2014. Such a delay would put the Amendment Bill on the agenda for consideration by the Parliament during the first session of 2015 where the focus will be on the Union Budget, possibly leading to further delays in the passage of the proposals into law.

The new insurance regulatory landscape in Morocco: setting-up, corporate/M&A transactions and portfolio transfers

A new insurance regulatory body has been set up in Morocco, affecting the licensing requirements for insurers seeking to enter the market. A brief summary is provided below.

Overview of the market

The Kingdom of Morocco is the third largest insurance market within the Arab world (after the UAE and Saudi Arabia). The insurance penetration rate is 3.1% of GDP and in this respect Morocco is the leading country within the Arab world.

Recently, a major reform occurred with the setting up of the “**Autorité de Contrôle des Assurances et de la Prévoyance Sociale**” or ACAPS, a new independent regulatory body instituted on 20 March 2014.

The ACAPS has authority to supervise (i) insurance and reinsurance activities which include regulatory capital requirements control, (ii) pensions, (iii) invalidity pensions and (iv) mandatory health insurance.

Insurer and reinsurer licensing requirements

To be licensed as an insurance or reinsurance company in the Kingdom of Morocco by the ACAPS requires the company to be either a limited liability company or a mutual company and have a minimum share capital. Applications must include specified corporate information (i.e. constitutional documents, list of group companies, management and governance structure, financial statements), major shareholders (in particular those holding directly or indirectly more than 30% of the shares) and the program of activities.

The Chairman of the ACAPS has authority to issue an advisory opinion regarding the application prior to the ACAPS Board meeting deciding on the licensing. The ACAPS is not bound to grant a license within a specific time period.

A license may only be granted to (i) companies governed by Moroccan law and whose registered office is located in Morocco and (ii) foreign companies duly recognized by the Kingdom of Morocco pursuant to a free trade agreement.

Share transfer and change of control

Any change in the majority, any transfer of more than 10% of the shares, as well as any transaction resulting directly or indirectly in the acquisition, of more than 30% of the shares of an insurer require the ACAPS prior approval.

The filing must include details of (i) the companies involved (i.e. details on the seller and the purchaser, shareholding structure, corporate governance), (ii) the transaction (i.e. deal structure and value) and (iii) the rationale of the transaction. The filing is less detailed in case of a transfer for less than 30% of the shares or which does not qualify as change in majority.

The ACAPS has 30 days to issue a decision from receipt of the filing. It may issue an objection if the transaction is considered to be contrary to public interest.

Merger and spin-off

Any merger or spin-off involving a licensed insurer or reinsurer is subject to the ACAPS prior approval. Any transaction is deemed to be approved in the

absence of a decision issued by the ACAPS following a 60-day period as from receipt of the application for consent.

As part of this process, the ACAPS may require the production of any document that may be necessary to assess the transaction before making its decision.

Portfolio transfer

A statutory process is available to implement a transfer of all or part of an insurance portfolio. Under such process, the insurer must file a request with the ACAPS and the policyholders and creditors of the insurer must be informed of the proposed transfer by way of a publication in an official gazette. They have three months within which to file any objection or comment.

Under this process, the ACAPS regulation committee must issue an opinion on the portfolio transfer, following which the ACAPS may then approve the transfer by publishing the approval in the aforementioned official gazette. The ACAPS cannot rule on the proposed portfolio transfer before the expiry of the three-month period described above.

To be approved, the filing must detail the insurance classes subject to the proposed portfolio transfer and include in particular (i) the draft portfolio transfer agreement, (ii) details of the assets and liabilities to be transferred (iii) details of the financials (including on technical provisions and solvency margins) of the companies involved and (iv) details of the administrative and technical resources of the transferee.

The portfolio transfer becomes enforceable towards policyholders as from the ACAPS approval. The process is based upon the French law approach.

Author: Victoria Sander

This publication is intended merely to highlight issues and not to be comprehensive, nor to provide legal advice. Should you have any questions on issues reported here or on other areas of law, please contact one of your regular contacts, or contact the editors.

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Contacts

For further information please contact:

Victoria Sander

Partner

(+44) 20 7456 3395

victoria.sander@linklaters.com

Wolfgang Krauel

Partner

(+49) 894 1808 199

wolfgang.krauel@linklaters.com

Matthew Middleditch

Partner

(+85) 2901 5352

matthew.middleditch@linklaters.com

Scott Sonnenblick

Partner

(+1) 212 903 9292

scott.sonnenblick@linklaters.com

Duncan Barber

Partner

(+44) 20 7456 3356

duncan.barber@linklaters.com

Dan Schuster-Woldan

Partner

(+44) 20 7456 5466

dan.schuster-woldan@linklaters.com

One Silk Street, London EC2Y 8HQ

Telephone (+44) 20 7456 2000

Facsimile (+44) 20 7456 2222

Linklaters.com