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Insurance Global – Autumn 2015

Introduction

Welcome to our first publication of Insurance Global. This half yearly publication highlights legal developments on the global horizon and outlines the key challenges facing both established and emerging insurance markets in the coming months.

Although insurance and reinsurance is increasingly global, the underpinning infrastructure supporting these markets is often localised. Clifford Chance, using its international offices based in over twenty different countries, highlights local legal knowledge in this publication. And, by outlining jurisdictional specific developments, demonstrates Clifford Chance's unique ability to deliver exceptional and up-to-date solutions for our local and global insurance clients.

The Autumn 2015 edition focuses on developments in the European sphere, namely the forthcoming Solvency II legislative package and the Insurance Distribution Directive, and on the global stage with legal updates from Germany, Italy, Luxembourg, Poland, Spain, the United Arab Emirates, the United Kingdom and the United States.

For further information on a particular topic, please get in touch – the contact details for the relevant office can be found in the global contacts page.

The Insurance Sector Team

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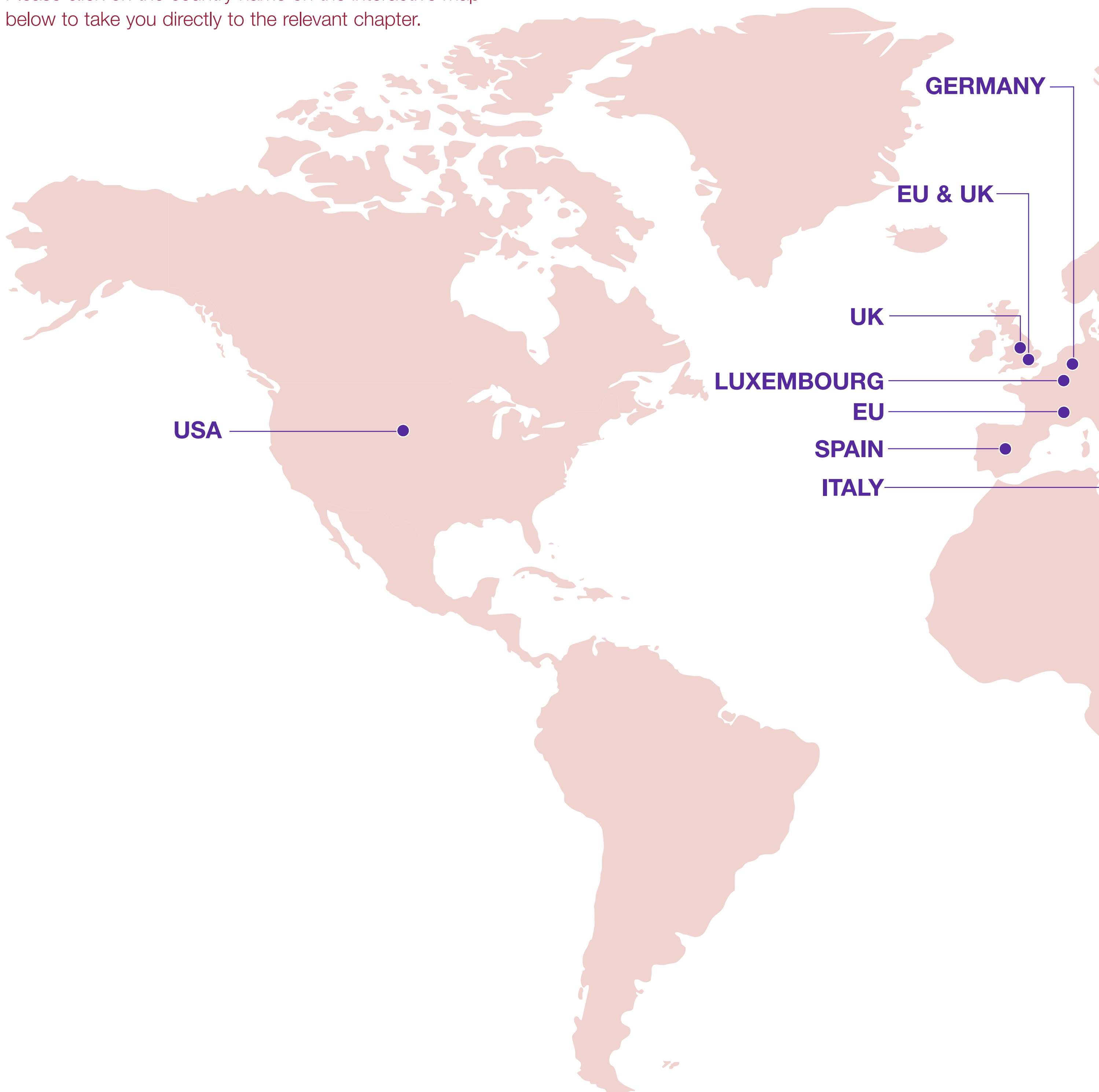
World Map

Please click on the country name on the interactive map below to take you directly to the relevant chapter.



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EU & UK

The Insurance Distribution Directive – final compromise text

On 17 July 2015, the European Council published the final compromise text of the Insurance Distribution Directive ("**IDD**"), formerly, the Second Insurance Mediation Directive (IMD2) or the recast IMD.

The IDD will amend and replace the Insurance Mediation Directive (2002/92/EC) ("IMD") and is aimed at:

- extending the scope of application to all distribution channels, including proportionate requirements for those who sell insurance products on an ancillary basis;
- identifying, managing and mitigating conflicts of interest;
- strengthening administrative sanctions, as well as measures to be applied in the event of a breach of key provisions;
- enhancing the suitability and objectiveness of insurance advice;
- ensuring that sellers' professional qualifications match the complexity of the products they sell; and
- clarifying the procedure for cross-border market entry.

The final compromise test is accompanied by a note from the Council which invites the Permanent Representatives Committee of the European Parliament ("**COREPER**") to approve the final compromise text regarding IDD and, subject to revision of that text by the legal linguists of both institutions, adopt its position at first reading as regards IDD. The Council will then approve the European Parliament's position and the IDD will be adopted in the wording which corresponds to the European Parliament's position.

On 22 July 2015, the Council of the EU published a press release confirming approval of the text through COREPER. The IDD will now be submitted to the European Parliament for a vote at first reading, before final consideration by the Council. The text has not been significantly amended since the publication of a revised 6th presidency compromise text dated 7 November 2014 and some of the latest key amendments include:

- the automatic exemption from providing certain information to professional customers no longer applies. Instead, Member States may choose to dis-apply those information requirements in the case of insurance-based investment products for such customers;
- clarification that reinsurance 'reinsurance distribution' does not include professional loss adjusting, expert appraisal of claims and the management of claims of a reinsurer; and
- the introduction of a power for the European Commission to specify criteria for assessing whether inducements have a detrimental impact on customer service and interests.

Impact in the UK

The implementation of IDD is unlikely to change the regulatory requirements for insurance mediation in the UK in relation to non-investment based insurance. This is because the UK implemented more stringent requirements to protect consumers on the implementation of IMD in 2002, which was a minimum harmonisation directive.

A detailed briefing note on the impact of the IDD is available here.

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"The implementation of IDD is unlikely to change the regulatory requirements for insurance mediation in the UK in relation to non-investment based insurance."

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EU

Solvency II Equivalence Update

On 5 June 2015, the European Commission adopted the first third-country equivalence decision under Solvency II, taking the form of non-legislative delegated acts affecting Switzerland, Australia, Bermuda, Brazil, Canada, Mexico and the USA.

The Swiss regime has been found to be equivalent in all three areas of Solvency II: solvency calculation; group supervision and reinsurance. Provisional equivalence in respect of solvency calculation has been granted for a period of 10 years for Australia, Bermuda (other than captives), Brazil, Canada, Mexico and the USA (the '**second package**').

The delegated acts cannot enter into force until the European Parliament and the Council have reviewed the decisions. The time limit for review is three months, with a possible three month extension. Equivalence as of 1 January 2016 will be jeopardised should the European Parliament adopt a resolution opposing the delegated acts or ask the Commission to withdraw or amend them.

In a letter to the European Commission dated 16 July 2015, the chair of the Economic and Monetary Affairs Committee, Roberto Gualtieri gave notice on behalf of the European Parliament that the deadline for raising objections to the delegated act for the second package is extended until 7 December 2015, without giving an explanation. This came as a surprise as the Commissions decisions were expected to be confirmed quickly by the European Parliament.

The reason behind the extension may relate to a letter to the Commission from Roberto Gualtieri dated 1 April 2015, in which he stated, on behalf of the EMAC, that the delegated acts for the second package were to be presented on a per-country and per-area basis, presumably to allow Parliament to object to some of the proposals but accept others at its discretion. The letter also asked for the draft acts to be presented before the end of April 2015. Neither request was met by the Commission nor was an explanation provided in the Commission's explanatory memorandum relating to the delegated act for the second package. Whilst certainty is good for both European and international insurance business, it is apparent that we will have to wait a little longer for clarity on this important aspect of the Solvency II regime.

EU Data Protection Regulation

The European institutions are well into the 'trialogue' discussions of the proposed new EU Data Protection Regulation, with much time being spent on trying to resolve the substantial differences between the proposals of the European Parliament and Council. However, good progress is being made in the discussions and it looks likely that the Regulation will be passed in 2016 and take effect in 2018.

Clifford Chance will produce a separate client briefing on the likely implications of the Regulation for the insurance industry, with publication expected in late 2016.

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Germany

Further relief for life insurers?

German life insurers are currently facing a challenging legal and economic environment. Not only do they need to get prepared for the start of Solvency II at the beginning of next year, but they also have to cope with low interest rates that are expected to prevail for some time. These circumstances draw into question the traditional business model of German life insurers under which they grant guaranteed interest rates for the entire term of endowment policies and may even endanger the existence of some of them.

Whereas challenges for German life insurers to meet solvency requirements under Solvency II in light of the long term guarantees granted to policyholders have been alleviated by transitional measures regarding the calculation of interest rates and technical provisions, there remain strains under German law.

In August 2014, the German legislator already became active in supporting life insurers. Under the Life Insurance Reform Act (*Lebensversicherungsreformgesetz*), it limited the insurers' obligation to pay out hidden reserves on fixed income securities to policyholders upon termination of their policy. Due to the decrease in interest rates, insurers have build up considerable hidden reserves and their statutory obligation to pay out half of the hidden reserves attributable to a policy had lead to an outflow of funds that increasingly threatened to weaken the companies inappropriately and discriminated against the remaining policyholders.

However, such measure may not be sufficient to make sure that German life insurers will get safely through the current challenges. In particular, the insurers' accounts are encumbered by the obligation to build up additional reserves if a market reference interest rate falls below the guaranteed interest rate under a policy. This obligation was introduced in 2011 in order to make sure that German life insurers will be able to meet their obligations to pay out guaranteed interest rates in the long run. However, the current long period of low interest rates triggers the need for additional reserves at a rate that may bring some of the market participants into distress. The insurance industry is therefore looking to the German government for further relief which may be granted by a reduction in the required additional reserves.

"German life insurers are currently facing a challenging legal and economic environment. Not only do they need to get prepared for the start of Solvency II at the beginning of next year, but they also have to cope with low interest rates that are expected to prevail for some time."

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Italy

IVASS consults on Solvency II implementing regulations

Further to the publication on the Italian Official Gazette of Legislative Decree no. 74 of 12 May 2015, implementing Solvency II in Italy and amending Legislative Decree no. 209 of 7 September 2005 (Italian Insurance Act), the *Istituto per la Vigilanza sulle Assicurazioni* ("**IVASS**") has published five consultation documents (the "**Consultation Documents**") on certain second level regulations intended to give full implementation to Solvency II in Italy, by also taking into account the relevant guidelines published by the European Insurance and Occupational Pensions Authority ("**EIOPA**").

Amongst other things, the Consultation Documents focus on the following:

- a new regulation on ancillary own funds, intended to implement the EIOPA's Guidelines on ancillary own funds (Consultation Document 1);
- a new regulation on ring-fenced funds and on the calculation of the notional Solvency Capital Requirement (SCR), intended to implement EIOPA's Guidelines on ring-fenced funds (Consultation Document 2);
- a new regulation on undertaking-specific parameters, intended to implement EIOPA's Guidelines on undertaking-specific parameters (Consultation Document 3);
- a new regulation on basis risk in the calculation for the Solvency Capital Requirement (SCR), intended to implement EIOPA's Guidelines on basis risk (Consultation Document 4); and
- a new regulation on loss-absorbing capacity of technical provisions and deferred taxes in the calculation of the Solvency Capital Requirement (SCR), intended to implement EIOPA's Guidelines on loss-absorbing capacity of technical provisions and deferred taxes (Consultation Document 5).

As to Consultation Documents 1, 3 and 4, comments are due by 31 August 2015 respectively at the following e-mail addresses: AOF@ivass.it; USP@ivass.it; SCR_BR@ivass.it.

As to Consultation Document 2, comments are due by 13 October 2015 at the following e-mail address: RFF@ivass.it.

As to Consultation Document 5, comments are due by 30 September 2015 at the following e-mail address: LAC@ivass.it.

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Luxembourg

Licensing and Operating Conditions for Insurance and Reinsurance Intermediaries and Insurance Sector Professionals

Grand Ducal Regulation of 27 July 2015

CAA Regulations No 14/01 of 1 April 2014 and 15/01 of 7 April 2015

A new Grand-Ducal Regulation dated 27 July 2015 modifying the Grand-Ducal Regulation of 8 October 2014 on licensing and operating conditions for insurance and reinsurance intermediaries as well as professionals of the insurance sector has been published in the Luxembourg official journal (*Mémorial A*).

The new Regulation provides that an examination jury is in charge of conducting the aptitude examination for (re-)insurance intermediaries and managers and provides for the composition of the examination jury and the nomination process for its members.

The new Regulation entered into force on and is applicable from 2 August 2015.

The new regime for aptitude examinations of (re-)insurance intermediaries and managers is completed by:

- Regulation No 14/01 issued by the Luxembourg insurance sector supervisory authority Commissariat aux Assurances ("**CAA**") on 1 April 2014 relating to aptitude examinations of (re-)insurance agents and insurance sub-brokers
- Regulation No 15/01 issued by the CAA on 7 April 2015 relating to aptitude examinations of (re-)insurance brokers and managers of broker companies.

The CAA Regulations No 14/01 and 15/01 foresees the details for the organisation and proceeding of these aptitude examinations and sets out the knowledge examined. CAA Regulation 15/01 is applicable as of the autumn 2015 examination session. CAA Regulation No 14/01 already applied since June 2014.

Life Insurance: Investment Rules for Unit-linked Life Insurance Products

CAA Circular 15/3

The CAA published on 27 March 2015 a new circular 15/3 regarding investment rules for unit-linked life insurance products. The new circular repeals, subject to a transitional regime, circular 08/1 on the same topic with effect on 1 May 2015.

The circular combines, amongst others, new rules on investments in "specialised insurance funds", being internal funds other than dedicated funds without a guaranteed return and linked to one underlying contract only. Further changes include the introduction of a five-category classification of subscribers on the basis of their wealth and the amount of premiums paid. The circular also modifies the rules for investments in alternative investment funds and structured deposits. Finally, it widens the scope of products into which collective internal funds available to high-net worth individuals may invest.

Life- and Non-life Insurance and Pension Funds: Deposit of Assets Representing Technical Reserves

CAA Circular 15/4

The CAA published on 24 March 2015 circular 15/4 on the deposit of securities and liquid assets used as assets representing technical reserves of direct insurance undertakings and pension funds subject to supervision by the CAA.

The new circular repeals, subject to a transitional regime, circular 09/7 on the same topic. The new circular further introduces certain new rules in respect of assets located with branches outside of the home country of the deposit bank and for deposit banks turning into branches of other credit institutions or turning back into independent institutions. The template deposit convention annexed to the circular reflects these revised rules.

The new circular entered into force on 1 May 2015.

Life Insurance: ACA Charter of Quality

CAA Circular 15/8

The CAA issued on 25 June 2015 circular 15/8 on the adoption of the Life Insurance Charter of Quality prepared by the Luxembourg Association of Insurance Undertakings (*Association des Compagnies d'Assurances* – ACA) in 2013 and updated in 2015.

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The ACA Life Insurance Charter of Quality is inspired by the ICMA Private Wealth Management Charter of Quality and is in line with the policy of transparency of the Luxembourg government.

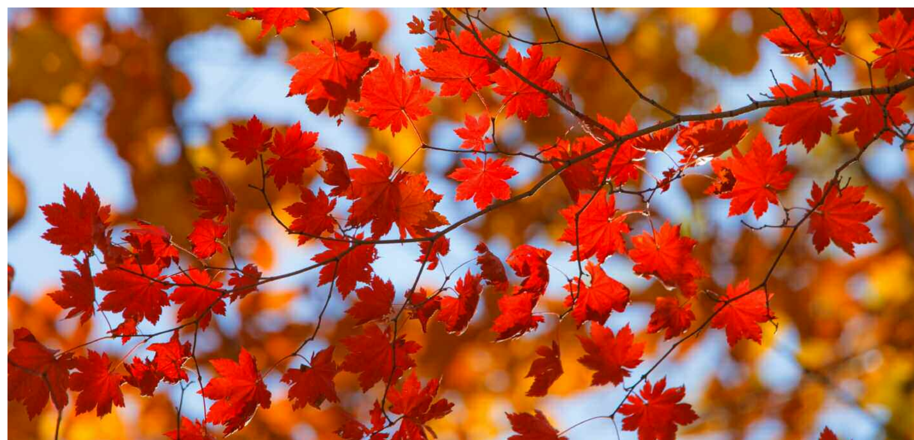
The CAA welcomes this initiative and strongly encourages all insurance undertakings to adopt and implement this charter. The circular therefore invites the management of the insurance undertakings to inform the CAA by 15 July 2015 whether their undertaking has adhered to the Charter. Where an insurance undertaking has not adhered to the Charter, the management will need to explain the reasons for such non-adherence.

Life- and Non-life Insurance and Reinsurance: New secured electronic transmission of reporting by insurance and reinsurance undertakings

CAA Circular 15/10

The CAA issued on 15 July 2015 circular 15/10 on the new secured electronic transmission of reporting by insurance and reinsurance undertakings to the CAA in light of the forthcoming entry into force of the Solvency II regime on 1 January 2016.

The new reporting by secured transmission channels specified in the circular will replace the current reporting via email. A test phase for the new transmission channels will run as of 15 October 2015 and further relevant information will be circulated before such date.



In order to efficiently implement this new reporting system, insurance and reinsurance undertakings, as well as auditors, must have:

- notified the CAA of their Legal Entity Identifier by 31 July 2015;
- requested (as the case may be) a CAA applicant code by 31 August 2015; and
- implemented one of the transmission channels proposed by the CAA and notify the CAA of their choice by 30 September 2015.

The CAA expects that the new reporting data transmission system will be fully operational by 15 December 2015.

Other Publications concerning the Insurance Sector

The CAA further issued the following documents:

- Information notice dated 14 January 2015 on reporting requirements under the Solvency II regime
- Information notice dated 21 January 2015 in relation to the Luxembourg law dated 28 July 2014 on the mandatory deposit and immobilisation of bearer shares and units.
- Circular 15/5 concerning the first set of Solvency II Guidelines published by EIOPA on 2 February 2015;
- Circular 15/6 on the reporting of professionals of the insurance sector (PSA);
- Circular 15/7 modifying and supplementing the amended circular letter 98/1 on technical interest rates; and
- Information notice dated 2 June 2015 on the implementation of the “Joint Guidelines on the convergence of supervisory practices relating to the consistency of supervisory coordination arrangements for financial conglomerates” issued by the Joint Committee of the European Supervisory Authorities on 22 December 2014.

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Poland

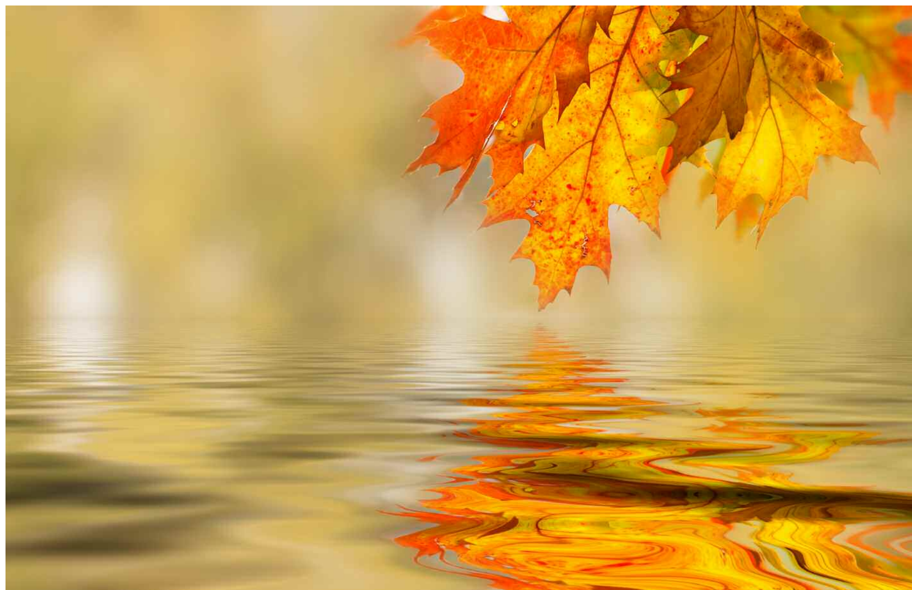
Proposed New Bill on Insurance and Re-Insurance Activity

A new bill on insurance and re-insurance activity recently proposed by the Polish government aims to introduce a new comprehensive regulation of insurance and reinsurance activity in Poland.

The bill will set out the conditions for providing personal, property and life insurance, and for running a reinsurance business, and is to replace the existing Act on Insurance Activities of 2003.

The main purpose of the bill is to implement into Polish law the Solvency II directive, which adopts the economic risk-based solvency regime, together with the 'total balance sheet' approach and focuses on proactive management of risks to ensure a uniform and enhanced level of policyholder protection within the EU.

The new bill also introduces a number of pro-consumer mechanisms, in particular concerning unit-linked life insurance contracts. In particular, it expands on the scope of information the customer must be provided with before a unit-linked life insurance contract is entered into; requires an insurance company to conduct an analysis of the needs of the policy holder or the insured before concluding an investment insurance agreement, for the purpose of evaluating what insurance agreement is appropriate for the policy holder or the insured; gives a life insurance policy holder a grace period, after entering into a contract, during which he or she may terminate the contract at minimum cost or no cost; and expands the role of out-of-court tribunals and bodies in the resolution of disputes between insurers and policy holders.



The bill is expected to be adopted before the end of the current term of the Parliament, i.e. autumn 2015, and to enter into effect on 1 January 2016.

"The new bill also introduces a number of pro-consumer mechanisms, in particular concerning unit-linked life insurance contracts."

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Spain

Law on implementation of Solvency II in Spain published in Official Gazette

The Law of management, supervision and solvency of insurance and reinsurance companies ("**Solvency II Law**"), which partially implements the EU Solvency II Directive (2009/138/EC) as amended by the Omnibus II Directive (2014/51/EU) (the "**Solvency II Directive**"), was published published in the Spanish Official Gazette on 15 July 2015.

Part of the Solvency II Directive will be implemented through a new Regulation of management, supervision and solvency of insurance and reinsurance companies (the "**Solvency II Regulation**"). A draft Solvency II Regulation has achieved a broad consensus and it is expected to be approved before the end of 2015.

The Solvency Law will enter into force on 1 January 2016 except for a few provisions related mainly to the process of adaptation to Solvency II or some of the amendments included in other laws of the insurance sector which enter into force before.

Generally speaking the Spanish implementation follows the wording of the Solvency II Directive literally.

The Solvency II Law does not reinforce the independence role of the General Directorate of Insurance and Pension Funds ("**DGSFP**") vis-à-vis the Ministry of Economy and Competitiveness ("**MineCo**"). However, the DGSFP has some new powers such as, for example, the ability to issue binding circulars in the scope of its supervisory regulatory powers. Fines for breaches of the Solvency II Law have also been toughened with regard to the previous law.

There are also changes for the mutual sector such as the possibility to set up mutual groups for solvency capital purposes and that mutual benefit companies, mutual companies and cooperative insurance entities with floating premiums will disappear and must be converted into another form of insurance entity.

The Solvency II Law has also been used to introduce other changes in insurance sector laws not related to the Solvency II process. In particular:

- the insurance contract law is amended to avoid a variation in the state of health of the insured being considered an increase in risk;
- tax laws are amended with the purpose of bringing them in line with the Judgment of the Court of Justice of the European Union, of 11 December 2014 in Case C – 678/11 which stated that it was contrary to European law to oblige EEA insurance entities which operate in Spain under free provision of services and EEA pension funds to have a tax representative in Spain; and
- the insurance mediation law is amended to reinforce fair analysis obligations of brokers by eliminating the presumption that fair analysis was correctly done if at least three different insurance offers were analysed, and to replace the figure of the external assistant of insurance intermediaries with the so-called 'collaborator' of insurance intermediaries.

The next step in the implementation of the Solvency II Directive is the Spanish Solvency II Regulation.

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"The Solvency II Law has also been used to introduce other changes in insurance sector laws not related to the Solvency II process."

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UAE

The Insurance Authority has issued Financial Regulations to Traditional and Takaful Insurance Companies.

(Decision No. (25) of 2014 Pertinent to Financial Regulations for Traditional Insurance Companies and Decision No. (26) of 2014 Pertinent to Financial Regulations for Takaful Insurance Companies)

Update

At the end of last year the UAE Insurance Authority (the "**Insurance Authority**") published its anticipated set of prudential regulations. The "**Financial Regulations**" create a new regime for the financial, technical, investment, and accounting operations of traditional and takaful insurers operating in the UAE, including branches of foreign insurers. The regulations have been combined in a single legislative instrument for traditional insurers and a separate instrument for takaful insurers, each comprising of the following seven key regulatory sections addressing the financial, technical, investment, and accounting aspects:

- the requirements and limits on investments;
- the solvency margin and minimum guarantee fund;
- calculations for technical provisions;
- determining the company's assets that meet the accrued insuring obligations;
- record keeping requirements and reporting requirements to the Insurance Authority;
- accounting and audit requirements; and
- accounting policies to be adopted and the necessary forms needed to prepare reports and financial statements and presentations.

Commentary

The Financial Regulations provide a relatively well advanced set of rules to introduce a risk based capital adequacy, provisioning and supervisory regime for insurers operating in the UAE and mark a fundamental shift in the supervision of insurers in the UAE.

The detailed requirements will need to be implemented by insurers, including those with only branches in the UAE, over the next one to three years and will involve:

- the development of systems to efficiently calculate solvency capital requirements and undertake enterprise risk management;
- consideration of the allocation of capital in its location, investment class, management and supervision; and
- enhancement of governance and controls to match the supervisory expectations of the new regime.

In meeting the requirements, insurers will need to introduce a significant amount of new policies and governance and controls and comply with detailed and frequent new reporting requirements. The key role of the actuary is at the forefront of the Financial Regulations and is likely to increase demand for actuarial resource in the UAE.

Of particular note regarding capital and investments would be the requirement, for a UAE-only insurer, to hold 50% of total investments and 100% of assets backing technical provisions in the UAE and a restriction on holding assets in a foreign jurisdiction with a sovereign rating which is worse than the sovereign rating of the UAE. There are equivalent restrictions for UAE branches of foreign insurers in respect of assets held to meet UAE insurance liabilities and solvency requirements. The investment limits outlined by asset class in Table 1 will apply.

With the added changes required in respect of accounting principles, the requirements outlined in Table 1 could be very significant for certain insurers with large investment exposures which may, in addition, need to be revalued upwards pursuant to new accounting requirements. Whilst the Financial Regulations provide for significant implementation periods in this area, the rules include requirements to report to the Insurance Authority during this period demonstrating progress in aligning operations to the new regime.

H. E. Eng. Sultan bin Saeed Al Mansouri, UAE Minister of Economy and Chairman of the Insurance Authority has commented that the Financial Regulations put the UAE at the forefront of the Middle East with regard to adopting the latest solvency requirements similar to the European model. We would agree and note the regulations avoid certain of the complexities behind Solvency II whilst introducing many of its core principles and adopts a Solvency I regime in certain areas.

For many insurers in the market, we consider that the Financial Regulations are a positive step forward for the UAE Insurance Authority and a platform for growth in this sector. The regulations will hopefully provide for a prudential regime which requires management to invest and reserve in a manner appropriate for the evolving risks in its operations and capital position but without inhibiting growth. For smaller insurers, the new requirements may be demanding and costly. We consider the Financial Regulations may suggest benefits in consolidation across

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the fragmented UAE insurance market by, among other things, supporting the diversification of risks and requiring the creation of systems and controls adapted to manage more complex organisations.

For foreign insurers active in the UAE, the Financial Regulations must be carefully reviewed against the location of capital allocated to the UAE and firms accessing the market by reinsuring the risks of a locally licenced insurer will need to evaluate the additional substance requirements (both in terms of capital requirements and governance and controls) as well as the impact of the reinsurance on the capital requirements in respect of credit risk (the new counterparty default risk module in the solvency template) for the local insurer.

For other foreign firms transacting with and advising local insurers, the new restrictions on their operations and investing capability, for example the restrictions on non-hedging derivatives, should be carefully considered as local firms will come under pressure from the Insurance Authority to evidence adjustments being made over the coming years.

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Table 1

Type of Invested Assets	The Maximum Limit of Total Exposure Cases in the Category of Certain Assets	The Maximum Sub-limit of the Exposure of a Certain Category of Relevant Assets
Real Estate	30%	**No sub-limit**
Equity instruments in the listed and unlisted companies in the financial markets within the State.	30%	**10%**
Equity instruments in the listed and unlisted companies in the financial markets outside the State.	20%	**10%**
Government securities and Sukuk issued by the State and/or issued by one of the Emirates.	100%	**25%**
Government securities/Sukuk issued by the foreign countries of class "A".	80%	**25%**
Cash and deposits with banks such as current accounts, demand deposits, term deposits, notice deposits, certificates of deposits and others inside the State.	5% as a minimum	**50%**
Loans secured by takaful insurance policies on persons (except the unit-linked insurance policies) issued by the company.	30%	**No sub-limit**
Financial derivatives or structured financial instruments compatible with the invested provisions of the Islamic Sharia'a and used for hedging purposes only.	1%	**No sub-limit**
Sukuk and deposits in other than banks as well as other debt instruments having a strong or very strong rating by a reputable and independent rating agency.	30%	**20%**
Other invested assets.	**10%**	**No sub-limit**

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UK

The PRA's Insurance Directors letter

On 14 July 2015, the PRA published a letter from the PRA's Insurance Directors (Andrew Bulley (Life) and Chris Moulder (General)) for all Solvency II-affected firms. The letter is a helpful update on the progress of Solvency II implementation in the UK.

The PRA confirms that, on 6 July 2015, the European Commission published the second set of both the draft Implementing Technical Standards ("**ITS**") and Level 3 Guidelines. The ITS have now been submitted to the European Commission for scrutiny and endorsement, whereas the Level 3 Guidelines are now subject to a 2 month 'comply and explain' process by national competent authorities. Further details on Solvency II implementation in the UK are detailed in the Solvency II: Spring 2015 update.

The PRA uses the letter to remind firms of the objectives of the new Senior Insurance Manager's Regime ("**SIMR**"), details of which are outlined in our SIMR update, and which implements Solvency II governance requirements so as to:

- ensure that all insurance firms and groups have a clear (and effective) governance structure; and
- clarify and enhance the accountability and responsibility of individual senior managers and directors.

Next steps

The PRA advises that, ahead of implementation, firms should carry out the following steps:

"Firms considering how the new Solvency II requirements will impact on them are encouraged to get in touch."

- familiarise themselves with the requirements of the new SIMR, including 'Prescribed Responsibilities'– high level PRA rules on senior insurance managers;
- prepare a governance map;
- identify which existing Controlled Functions ("**CF**") roles will 'grandfather' into the SIMR – for grandfathering to apply, the individual must be performing the same function both at the date of notification to the PRA and on 7 March 2016; and
- consider whether there are other individuals who are not currently approved as CFs but will be performing a Senior Insurance Manager Function ("**SIMF**") under the SIMR, or who will be a deemed to be a 'key function holder'.

Given the extensive group regime under Solvency II, the PRA also advises that, as a matter of urgency, firm's who have not already done so should establish:

- whether they are part of a group, or groups, that fall within the scope of Solvency II;
- if they are part of group, what type of group(s) they will be a part of e.g. a group headed by an insurance holding company or a mixed activity insurance holding company;
- what they will need to do to meet all the requirements of Solvency II; and
- what approvals and/or waivers they might require to assist them in complying with the groups requirements of Solvency II.

The group considerations for firms are complex and could be further complicated by equivalence considerations (see our Solvency II equivalence briefing).

Clifford Chance has advised extensively on Solvency II group structuring and equivalence issues and is assisting firms to meet the new SIMR requirements. Firms considering how the new Solvency II requirements will impact on them are encouraged to get in touch.

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USA

A New Bill Clarifying the Insurance Exception to the PFIC Rules

On June 25 2015, Senate Finance Committee Ranking Member Ron Wyden introduced a bill (the "Bill") that will require insurance companies to maintain minimum levels of certain insurance liabilities in order to qualify for the exception to the passive foreign investment company ("PFIC") rules applicable to insurance companies.

The "PFIC" rules generally require US shareholders in a PFIC to take into account their share of the PFIC's income currently in order to avoid generally unfavorable tax consequences when those US shareholders sell their PFIC stock or receive certain distributions from the PFIC. A foreign corporation is a PFIC if it owns passive assets or receives passive income above certain thresholds. However, in recognition of the key role that passive income plays in the operation of an insurance business, the PFIC rules contain an exception for passive income "derived in the active conduct of an insurance business" (the "Insurance Exception"). The exact contours of this rule are largely undefined, but legislative proposals, including a proposal last year from Representative David Camp and the current proposal from Senator Wyden, would provide further clarity.

Under the terms of the Bill, in order to qualify for the Insurance Exception, in addition to being actively engaged in an insurance business, a foreign company must have "applicable insurance liabilities" that constitute more than 25% of its total assets. If the company fails this bright-line test, it may still temporarily qualify for the Insurance Exception, but only if the company's applicable insurance liabilities constitute more than 10% of the company's total assets, and, based on the facts and circumstances:

(i) the company's failure to satisfy the 25% test is due solely to temporary circumstances involving the insurance business, and

(ii) the company is predominantly engaged in the insurance business.

A company with applicable insurance liabilities that constitute less than 10% of its total assets would not qualify for the Insurance Exception.

Further background information and detailed Bill proposals can be found in our June 2015 briefing note.

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