



BANK OF ENGLAND
PRUDENTIAL REGULATION
AUTHORITY

Consultation Paper | CP38/16

Solvency II: group supervision

November 2016

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Responses are requested by Tuesday 7 February 2017.

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1 Overview

1.1 In this consultation paper (CP), the Prudential Regulation Authority (PRA) sets out proposals to update Supervisory Statement (SS) 9/15 ‘Solvency II: group supervision’¹ to reflect some of the Solvency II (‘the Directive’)² material previously set out in the PRA’s letter ‘Solvency II: An update on implementation’ published on 25 July 2014.³ It also sets out proposals to update SS9/15 to take account of certain aspects of the Solvency 2 Regulations 2015 (‘the Regulations’),⁴ and to update it with references to the PRA Rulebook.

1.2 This consultation is relevant to all insurance firms within the scope of the Directive and to Lloyd’s.

Background

1.3 SS9/15 was published in March 2015, prior to the implementation of the Directive. Following this, the PRA published the Directors’ letters in the period prior to (and shortly after) the Directive came into effect to share information, including its developing thinking on issues generated by firms during their preparation for Solvency II, as quickly and as transparently as possible. This ensured that all firms had access to the information they were likely to need to prepare for compliance with the Directive from 1 January 2016.

1.4 The PRA has now reviewed the Directors’ letters and has considered the extent to which any of that preparatory material should be carried forward, post-implementation of Solvency II, to become ongoing supervisory expectations of firms in the context of group supervision. In the relatively limited areas where this is the case, the PRA proposes to update SS9/15 to incorporate that material, so that it is available for firms to reference in a format that aligns with the PRA’s supervisory approach, and to allow firms an opportunity to comment on these proposals. These proposals follow on from CP20/16 ‘Solvency II: consolidation of Directors’ letters’ published in May 2016.⁵

1.5 On publication of the final supervisory statements, the Directors’ letters that inform this consultation will be archived.

Structure of the CP

1.6 As noted above, ‘Solvency II: An update on implementation’ published on 25 July 2014 was used for the proposed amendments to SS9/15 (see appendix).

Responses and next steps

1.7 This consultation closes on Tuesday 7 February 2017. The PRA invites feedback on the proposals set out in this consultation. Please address any comments or enquiries to CP38_16@bankofengland.co.uk.

1 March 2015; www.bankofengland.co.uk/pr/Pages/publications/ss/2015/ss915.aspx.

2 Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (recast).

3 www.bankofengland.co.uk/pr/Documents/solvency2/solvency2updatejuly2014.pdf.

4 SI 2015/575 available at www.legislation.gov.uk/ukSI/2015/575/contents/made.

5 www.bankofengland.co.uk/pr/Pages/publications/cp/2016/cp2016.aspx.

2 Proposals

2.1 The proposals in this CP are intended to clarify for firms which aspects of the PRA's letter 'Solvency II: An update on implementation' published on 25 July 2014 on group supervision are now intended to have effect as ongoing supervisory expectations. The CP also includes proposals to address elements of the Solvency II legislation introduced after the publication of the relevant letters; including the Regulations and to update it with references to the PRA Rulebook.

2.2 These proposals will result in the consolidation of PRA expectations in respect of Solvency II group supervision as they are intended to be implemented in the form of an update to the current SS9/15.

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2.3 The PRA proposes to update SS9/15 with a section on the availability of group own funds, expanding on what the PRA expects from firms when it calculates the own funds available to the group. It sets out the PRA's expectations for firms to:

- provide evidence of the absence of legal and regulatory restrictions on the transferability of own funds; and
- demonstrate that group own funds can be made available to the group within nine months.

2.4 Chapter 5 in SS9/15 on centralised risk management is proposed to be removed as the content is already included in Regulation 52 and Schedule 4 of the Regulations.

2.5 Other changes are designed to update or include relevant cross-references to the PRA Rulebook and the Directive requirements and to clarify the nature of, and processes for, making applications to the PRA for group capital add-ons and for 'other methods' of group supervision in the absence of third-country equivalence.

3 The PRA's statutory obligations

3.1 The PRA has a public law duty to consult widely on any measures that significantly affect firms. In discharging its general functions the PRA must, as far as it is reasonably possible, act in a way that advances its general objective, insurance objective, and secondary competition objective.

Compatibility with the PRA's objectives

3.2 The PRA considers that the proposals in this CP are compatible with the PRA's statutory objectives to promote the safety and soundness of PRA-authorized firms;¹ and in the context of insurance, to contribute to policyholder protection.² By providing guidance to firms on how the PRA expects firms to implement the Directive, the PRA is ensuring the main objective of the Directive, described in Article 27, as the protection of policyholders and beneficiaries, is met.

¹ Sections 2B(1) and 2B(2) of FSMA.

² Section 2C of FSMA.

3.3 The PRA also has a duty to facilitate effective competition as a secondary objective to its general safety and soundness and insurance objectives. The PRA has assessed whether the proposals in this CP facilitate effective competition and does not expect the proposals to have any material effect on competition. The effect on competition of the implementation of the Directive has already been considered in the Financial Services Authority's (FSA's) CP11/22 'Transposition of Solvency II Part 1'¹ and the PRA's CP16/14 'Transposition of Solvency II: Part 3'.²

Regulatory principles

3.4 In making its rules and establishing its policy, practices and procedures, the PRA must have regard to the regulatory principles as set out in the Financial Services and Markets Act 2000 (FSMA).³ Three of the principles are of particular relevance to this consultation:

- (i) that a burden or restriction which is imposed on a person, or on the carrying on of an activity, should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction. The PRA has followed this principle in consolidating its current expectations thereby making the information more accessible to firms;
- (ii) the desirability in appropriate cases of each regulator publishing information relating to persons on whom requirements are imposed by or under this Act, or requiring such persons to publish information, as a means of contributing to the advancement by each regulator of its objectives. The PRA has followed this principle by updating its original supervisory statement on group supervision (SS9/15) as soon as possible after the implementation of the Directive; and
- (iii) that the regulators should exercise their functions as transparently as possible. The PRA has followed this principle by issuing a consultation on its current supervisory expectations, and when the policy is finalised by archiving the historic documents and including links to where any new material can be found.

Cost benefit analysis

3.5 The overall economic effects of the proposals in the original supervisory statement have been considered previously, in the FSA's CP11/22 and the PRA's CP16/14.

3.6 The proposed draft supervisory statement clarifies the PRA's expectations of firms, but should not impose additional costs on firms, as the substance of the PRA's expectations contained within the statement has been issued previously in the form of Directors' letters, so firms should already be familiar with the proposals.

Impact on mutuals

3.7 When making general policy, the PRA considers whether, in its opinion, the impact of the proposed rules on mutuals will be significantly different from the impact on other firms. In the PRA's opinion, the impact of the revised supervisory statement on mutuals is expected to be no different from the impact on other firms.

1 November 2011; www.bankofengland.co.uk/publications/Documents/other/pr/policy/2013/transpositionofsolvency2-1cp11-22.pdf.

2 August 2014; www.bankofengland.co.uk/pr/pages/publications/cp/2014/cp1614.aspx.

3 Sections 2H(2) and 3B of FSMA.

Equality and diversity

3.8 The PRA is also required by the Equality Act 2010¹ to have due regard to the need to eliminate discrimination and to promote equality of opportunity in carrying out its policies, services and functions. The PRA has performed an assessment of the policy proposals and does not consider that the proposals give rise to equality and diversity implications.

¹ Section 149.

Appendix: Draft amendments to Supervisory Statement 9/15 'Solvency II: group supervision'

This appendix outlines proposed amendments to SS9/15 'Solvency II: group supervision'.

Underlining indicates new text and striking through indicates deleted text. Paragraphs following the deleted text in Chapter 1 have not been renumbered. Chapter 5 has been deleted and replaced with a new Chapter 5A. All the other chapters have been included in their entirety in order to assist the reader.

1 Introduction

1.1 This supervisory statement is addressed to all UK Solvency II firms ~~that are part of a group (and to the Society of Lloyd's, which the PRA considers to be as a mixed activity insurance holding company).~~ It sets out the Prudential Regulation Authority's (PRA's) expectations in respect of the Solvency II groups provisions.

1.2 [Deleted.]

1.3 This supervisory statement should be read in conjunction with the relevant European legislation, the Group Supervision Part of the PRA Rulebook, The Solvency 2 Regulations 2015¹ ('the Regulations') and the PRA's insurance approach document.² ~~The groups provisions referred to in this statement should be read alongside the relevant European legislation, which includes Articles 213 to 246, 256, 256a, 257 and 260 to 266 of the Directive. It should also be read in conjunction with the Solvency II Regulations, the rules in the Group Supervision Part of the PRA Rulebook and the high-level expectations outlined in the PRA's approach to insurance supervision.~~

1.4 This supervisory statement expands on the PRA's general approach as set out in its insurance approach document.³ 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 [Deleted.]

1.6 Firms should note that if the group supervisor is a supervisory authority other than the PRA, the PRA still expects UK insurers to comply with the groups provisions set out in Solvency II ('the Directive')⁴ and PRA rules relating to group supervision (to the extent applicable).

1 SI 2015/575 available at www.legislation.gov.uk/uksi/2015/575/contents/made.

2 Available at www.bankofengland.co.uk/publications/Pages/other/prasupervisoryapproach.aspx.

3 The Prudential Regulation Authority's approach to insurance supervision, June 2014; available at www.bankofengland.co.uk/publications/Pages/other/prasupervisoryapproach.aspx.

4 Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (recast).

2 Entities excluded from the scope of group supervision

2.1 Where a group, for which the PRA is the group supervisor, wishes to exclude entities from the scope of group supervision, it will be expected to make a formal application to the PRA. Where that application is approved, the exclusion will be given effect by the PRA issuing a direction under section 138A of the Financial Services and Markets Act 2000 (FSMA), taking into account the criteria in Article 214(2) of the Directive. The PRA expects ~~this~~ such applications to articulate the way in which the firm believes that the conditions set out in Article 214(2) of the Directive are met.

2.2 The PRA will assess applications to exclude entities from the scope of group supervision under Article 214(2) of the Directive on a case-by-case basis, and will consult ~~The PRA expects to only grant a waiver with respect to undertakings where it is satisfied that conditions Article 214(2) of the Directive are met, following a consultation with other~~ the concerned supervisory authorities in the circumstances required by Regulation 12 of the Regulations.

3 Choice of calculation method

3.1 Where the PRA is the group supervisor, ~~Article 220 of the Directive allows~~ the PRA may ~~to~~ decide, after consulting ~~the~~ other concerned supervisory authorities where relevant and the group (as required by Regulation 16 of the Regulations), to apply to the group either method 2 (deduction and aggregation method) or a combination of methods 1 and 2, where the exclusive application of method 1 (accounting consolidation-based method) would not be appropriate,¹ having considered the provisions of Article 328(1) of the Commission Delegated Regulation.² Where a group for which the PRA is the group supervisor wishes to use method 2 or a combination of methods 1 and 2, it will be expected to make a formal application to the PRA for a direction under section 138A of FSMA. The PRA expects this application to articulate the way in which the firm believes that the elements in Article 328(1) of the Commission Delegated Regulation should be considered in the context of the firm's application.

4 Group capital add-on

4.1 Where the PRA is the group supervisor, in considering whether the consolidated group solvency capital requirement (SCR) appropriately reflects the risk profile of the group, it may consider a capital add-on for a group if the circumstances referred to in Article 37(1)(a) to (d) of the Directive arise at the group level.

4.2 In particular, the PRA will consider imposing a capital add-on under Article 232 of the Directive where:

- (a) a specific risk at group level is not sufficiently covered by the standard formula or an internal model; or
- (b) a capital add-on is imposed on a Solvency II undertaking in the insurance group because its risk profile deviates significantly from the assumptions underlying the group's internal model.

1 Group Supervision 7 in the PRA Rulebook.

2 Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) Text with EEA relevance.

5 [Deleted.]

5A Availability of group own funds

5.1A Group Supervision 9.4 and Article 330 of the Commission Delegated Regulation¹ place limits on the own funds which can be included in the group solvency calculation, depending on their availability to absorb losses anywhere in the group. The PRA expects firms to be able to provide an analysis of such availability so that the PRA can assess the extent to which such own funds are eligible for inclusion (in accordance with Article 330 of the Commission Delegated Regulation). This analysis should form part of the annual solvency and financial condition report (Article 297(1)(h) of the Commission Delegated Regulation) and the regular supervisory report (RSR) (Article 311(1) and (6) of the Commission Delegated Regulation). The PRA also expects this analysis to be available to support the solvency position reported at each reporting date.

5.2A While this chapter only provides the PRA's expectations of firms in regard to Article 330, the PRA reminds firms that they will also need to classify separately own funds at group level in accordance with Articles 331 to 334.

5.3A At the group level, firms can take a number of potential actions to transfer own funds around the group, for instance through paying dividends, or selling the assets of an undertaking. The PRA will consider these actions when reviewing a group's assessment of transferability. However, the PRA expects groups to provide robust and credible evidence that the apparent availability of own funds at the group level is not compromised or effectively undermined by any legal or regulatory restrictions on transferability, and that the suggested action resulting in the transfer of the own funds does not jeopardise an orderly resolution of the group. In particular, the PRA expects the evidence to cover, as a minimum, the likely scenarios under which the actions could be taken, and the time that would be required to execute the actions. For the own funds considered available at group level, the PRA expects groups to evidence that these own funds can be made available to the group within a maximum of nine months.² Some groups appear to have considered only the legal restrictions when providing information to the PRA on the availability of own funds at the group level. However, the PRA expects groups to consider both legal and regulatory restrictions when considering any limitations on availability.

5.4A Under Solvency II, the PRA may decide to apply to a group the deduction and aggregation method (method 2) for calculation of its solvency requirements, which would allow a firm to use local solvency rules when determining the requirements placed on (equivalent) third-country related undertakings. However, the assessment of the availability at a group level of an own funds item of such a related undertaking needs to be carried out by reference to the Solvency II groups provisions, not merely local rules.

5.5A To illustrate this point further, the assessment of availability will need to demonstrate that both the solo undertaking third-country rules and the Solvency II group rules have been considered. For example, this might mean that for an own funds item to be considered available at the level of the group, the firm should be able to defer coupon payments both in

1 Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (Text with EEA relevance).

2 Article 330 of the Commission Delegated Regulation (EU) 2015/35.

the event of non-compliance with the solo undertaking's third-country capital requirement and the Solvency II group SCR.

6 Single own risk and solvency assessment report

6.1 A group, for which the PRA is the group supervisor, may apply to produce a single document covering its own risk and solvency assessments (ORSA) at the level of the group and at the level of any subsidiary in the group at the same time (Group Supervision 17.2(3)). The PRA will assess applications to produce a single ORSA document in consultation with the college of supervisors.

6.2 In addition to the ORSA conducted at group level, the PRA expects the group-wide ORSA document to include sufficient details on the solo firms included within the scope of the group-wide ORSA such that ~~Article 45 of the Directive~~ Conditions Governing Business 3.8 (solo ORSA) is satisfied in respect of each of those firms.

7 Single solvency and financial condition report

7.1 A group, for which the PRA is the group supervisor, may apply to produce a single report on its solvency and financial condition (SFCR) at the level of the group, and at the level of any subsidiary in the group which must be individually identifiable (Group Supervision 18.1(2)). The PRA will assess applications to produce a single SFCR in consultation with the college of supervisors.

7.2 The PRA expects the single document produced to cover the same level of detail on the solo subsidiary firms as is required in the solo SFCR.

8 Responsibilities of the relevant insurance group undertaking¹

~~8.1 Where the PRA is the group supervisor it may determine, after consulting the relevant supervisory authorities, the relevant insurance group undertaking in accordance with Article 219, which will be responsible for the group solvency calculations referred to in Article 218(2) and (3) of the Directive. [Deleted.]~~

8.2 For a group, for which the PRA is the group supervisor, it is sufficient for one relevant insurance group undertaking within an insurance group to undertake the following activities on behalf of the group to:

- (a) submit the relevant data for and the results of the group eligible own funds and the group SCR to the PRA, as referred to in Group Supervision 5.2;
- (b) ensure ongoing compliance with the conditions for the prudent management of subsidiaries, where the PRA has agreed to the use of a single document, the production of a the single document covering all relevant ORSAs and the production of a the single SFCR, as referred to in Group Supervision 15.4(2);
- (c) inform the PRA in an event of non-compliance with the group SCR within the appropriate timeframes, as referred to in Group Supervision 4.4; and

¹ Group Supervision 1 in the PRA Rulebook.

- (d) submit a realistic recovery plan and take measures to ensure compliance with the group SCR in an event of non-compliance with the group SCR within the appropriate timeframes, as referred to in Group Supervision 4.4.;
- ~~(e) to inform the PRA and the supervisory authorities of the subsidiary undertakings concerned of non-compliance with the centralised risk management (CRM) criteria, as referred to in Group Supervision 15.4(2)(a); and~~
- ~~(f) to present a plan on how compliance will be restored with the CRM criteria to the PRA and the supervisory authorities, as referred to in Group Supervision 15.4(2)(b).~~

9 Supervision in the absence of third-country equivalence

9.1 In the absence of equivalent group supervision, in accordance with ~~in accordance with Article 262 of the Directive~~ Group Supervision 20 the PRA may decide to apply to the group either the relevant Solvency II requirements will apply to the worldwide group as if it were based in the European Economic Area (EEA), or it may use, unless the PRA has specified 'other methods' ~~specified by the Directive pursuant to~~ to achieve the objectives of group supervision (Group Supervision 20). In the absence of a decision ~~from~~ by the PRA to apply specify 'other methods' ~~to~~ for the group, then firms in that group are required to apply the relevant Solvency II requirements to the worldwide group as if it were based in the EEA.

9.2 ~~Firms may apply to the PRA for a waiver from the requirement to apply the relevant Solvency II requirements to the worldwide group as if it were a group based in the EEA. Firms will be expected to make a formal application to the PRA, where they wish the PRA to specify 'other methods' for the purposes of Group Supervision 20.1(2). Any such specification will be given effect by the PRA issuing a direction under section 138A FSMA. In its application, the PRA expects a firms should to propose state other methods for the PRA to consider. Firms wishing to apply for a waiver direction should may do so via using the usual waiver and modification process. The PRA will assess such applications on a case-by-case basis, taking into account the objectives of group supervision as specified by the Directive.~~

9.3 If firms wish to submit an application before a relevant equivalence decision is made, they may do so stating the assumptions made with regard to equivalence. Where appropriate, the PRA may refrain from making a decision until an equivalence decision has been finalised.