

GUERNSEY ISSUES SPI RULES

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Guernsey has new rules for special purpose insurers. Mark Helyar, the lawyer and director who drafted the rules together with the Guernsey International Insurance Association, comments on this development and contrasts it with competition from other domiciles.

Guernsey's new rules for special purpose insurers (SPI) were issued by the Guernsey Financial Services Commission on January 1, signalling Guernsey's intention to remain at the forefront of growth in the insurance-linked securities (ILS) sector in 2017.

The first thing to note about Guernsey's ILS sector is that it has reached a substantial size without the need for SPI rules. Effectively the rules codify the discretions already applied by Guernsey's regulator under existing legislation which has been in existence since 2002.

Comparing Guernsey's approach to, for example, Bermuda's, has been difficult because of the lack of transparent, independent guidance about how ILS works and is licensed and regulated. This has been an area which competitors are keen to highlight to potential clients because it has enabled them to imply a lack of certainty, which is not a true reflection of the regulatory approach in Guernsey. Those 'in the know' were already familiar with the content, but now it is available to all.

The rules are designed to be focused squarely at the key commercial questions which arise for organisations and funds which look to structure or invest in ILS, namely;

- How much capital do I need? - none
- What can I use as collateral? - generally cash and category 1 LOC's, other assets on a discretionary basis
- How much will it cost? - set out (and reducing for cells as a result of recent consultation)
- How quickly can I move to close deals? - very quickly indeed
- Can I have pre-approved deals? - yes

As well as this there is comprehensive guidance on other important issues such as;

- Can I dividend / redeem and distribute capital and profits without procedural complexity? - yes
- How easy is it to talk to the regulator? - there is a short chain of command and a supportive, open regulatory environment

The new rules and guidance have also given rise to some other amendments – an SPI insurer is now formally recognised as a category 6 insurer for Guernsey regulatory purposes, which negates the need for certain regulatory requirements applicable to other types of insurer such as minimum capitalisation and returns in relation to solvency assessment. This approach properly reflects the risks associated with SPI vehicles, where typically 100% of the possible loss associated with underwriting a reinsurance contract is held in a trust account independent of the SPI vehicle.

This places Guernsey at least on the same footing as Bermuda in the European time zone for ILS transactions. Other places such as Gibraltar have issued guidance but there is no business traction.

There has been much recent commentary of onshore ILS in London, there are a number of key strategic and commercial factors which mitigate against this becoming a reality – the first is that the FCA has long chains of command and control and cannot hope to meet a three-day turnaround or less. Most ILS deals are compressed into very short periods around renewal and need to be conducted in hours rather than months.

Could this be achieved onshore? Well, nothing is impossible but there is a significant regulatory risk factor for London which is being ignored. The truth which dare not speak its name is that offshore jurisdictions providing administration services, such as Guernsey, are better regulated and have been for more than a decade. ILS structures ideally need independent organisations to run and administer them. This type of professional service industry is the bread-and-butter of the offshore world.

In Guernsey, as in Bermuda, insurance managers, fiduciary providers and directors are all licensed and directly regulated and for this reason their competence is well known to the regulators and responsibilities can be bestowed in the knowledge that regulatory sanctions, fines and disqualifications are readily available. The regulation of fiduciary and other service providers guarantees a high level of professionalism and competence and means that an offshore regulator which allows an insurance manager to assume responsibility is taking less risk than an onshore regulator where no such regulation exists. Would it be a sensible regulatory approach for the FCA to consider adding risk by rubber stamping short-term approvals for ILS structures managed by unregulated entities?

Even if all of the other hurdles can be overcome onshore, given that Insurance Premium Tax (IPT) has doubled in 18 months and there is talk of it rising to 20%, what is the likelihood of a nascent ILS industry in London remaining tax free were it to become successful? There is a very long precedent for successful industries to be taxed.

Whatever the outcome, the possibilities are obviously still expanding. Guernsey is now even better placed to take advantage of ILS business in the European time zone.

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