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NEW RULES AS GUERNSEY EVOLVES ITS ILS REGIME

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New rules for Special Purpose Insurers (SPIs) in Guernsey demonstrate the jurisdiction's intention to remain at the forefront of growth in the insurance-linked securities (ILS) sector, writes Dominic Wheatley of Guernsey Finance.

The Insurance Business (Special Purpose Insurer) Rules 2016 came into effect on 1 January 2017 and see the Guernsey Financial Services Commission (GFSC) clarify the regulatory treatment of collateralized reinsurance, including ILS.

The rules allow an applicant for the licensing of a new SPI to be granted a single consent for the formation of further SPIs without call for further application. The streamlined application process now allows new insurers to be established within one business day.

The Insurance Business (Solvency) Rules 2015 have also been amended to expressly include the new class of insurer. Under the new rules an SPI is not required to maintain the minimum or prescribed capital requirements, nor to conduct its own risk or solvency assessments. 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.

Mark Helyar, Of Counsel at Bedell Cristin, who drafted the rules in collaboration with the GFSC and the Guernsey International Insurance Association (GIIA), explains the new rules effectively codify the discretions already applied by Guernsey's regulator under existing 2002 legislation.

"Those 'in the know' were already familiar with the Guernsey's approach in this area, but the new SPI rules make it available to all. Previously, comparing Guernsey's approach to, for example, Bermuda, had been difficult because of the lack of transparent, independent guidance about how ILS works and is licensed and regulated. It had been an area which competitors were keen to highlight to potential clients because it enabled them to imply a lack of certainty, but that was never a true reflection of the regulatory approach in Guernsey," said Helyar.

SPIs must be fully collateralised to the extent of their liabilities and, in addition to ILS, may include collateralised reinsurance, catastrophe bonds, side-cars and life based securitisations.

Typically, cash assets will be applied against liabilities. However, under the changes, the GFSC recognises that the commercial interests of the counterparties may be satisfied using (re)insurance, letters of credit or partly paid shares. These changes demonstrate Guernsey's equivalence of approach to Bermuda as an alternative jurisdiction within the European time zone.

Those already familiar with Guernsey will not be surprised by the jurisdiction's nimble ability to innovate and evolve the ILS product. After all, 2017 marks the 20th anniversary since Guernsey conceived and introduced the Protected Cell Company (PCC) to the world for use in the captive insurance sector. The subsequent success of this innovation, as well as the later introduction of the Incorporated Cell Company (ICC), is illustrated by the fact that the cell company is now used across the financial services world as an alternative application for the structuring of many different types of products.

The fact that Guernsey pioneered the cell company concept means that the island has developed significant experience in this area and is now putting that expertise to use in its ILS offering where Guernsey's long track record in the investment funds and insurance space are combined.

As such, Guernsey acts as a centre where fund managers and promoters with capital to deploy are brought together with the transformation managers who understand insurance risk.

Indeed, the island's funds industry is so well-regarded that Guernsey remains the global leader for non-UK listed entities on the London Stock Exchange. Vehicles established in the island can also access other global capital markets, including the exchanges in Frankfurt, Ireland, Toronto, Australia, Hong Kong and Euronext, among many others, as well as the Channel Islands Securities Exchange (CISE), which is based in Guernsey.

In fact, in 2012, the CISE became home to the first private catastrophe bond listed on any exchange worldwide. Upon the listing of Solidum Re Eiger IC Limited on the CISE, Cedric Edmonds, Partner at Zurich-based Solidum Partners and Director of Solidum Re Eiger IC Limited, extolled the virtues of Guernsey as an ILS destination by highlighting its ICC legislation and the quality and 'can do' attitude of its service providers when faced with something new.

Conclusion

There are a number of outstanding factors which mean that Guernsey provides a unique proposition as a hub for ILS business.

This is already being recognised by many in the market and we expect that this growth will continue, particularly with the introduction of SPI rules, which clarify the regulatory treatment of collateralised reinsurance, including ILS. The innovative update highlights Guernsey's ability to find sensible, proportionate regulatory responses to the necessary but growing compliance burden on financial services organisations.

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