WRITTEN BY DOMINIC WHEATLEY

PCCS – 20 YEARS THAT SHOW GUERNSEY'S REPUTATION FOR INNOVATION

05 JUNE 2017

Guernsey Finance Chief Executive Dominic Wheatley reflects on Guernsey's success with PCC funds and the region's innovative spirit.

Other jurisdictions have changed the name in an attempt to differentiate, but effectively all cell company legislation globally has been based on that which was originally formulated in Guernsey 20 years ago.

Indeed, when talking about Guernsey's success stories in the world of financial services, few can match our pioneering introduction of the protected cell company (PCC) back in 1997.

The legislation, the Protected Cell Companies Ordinance, 1997, is widely-regarded as Guernsey's go-to example for financial innovation – a reputation we maintain to this day with products such as the Manager Led Product and the Private Investment Fund launching in the past year, and the island being home to the first commercial deployment of blockchain technology in the private equity market back in February.

Expertise

Indeed, with Guernsey being the first to adopt the cell company concept, the island has developed a world-class infrastructure for its application, supported by a range of lawyers and accountants with the highest level of expertise and experience in utilising the structure.

Aon's White Rock Insurance Company PCC Limited, which was established in Guernsey in 1997 as the first PCC in the world, has now been used by more than 100 corporations as a cell captive facility and has grown to be the largest structure of its kind globally.

Stewart McLaughlin, executive director at Aon Insurance Managers (Guernsey) and someone very familiar with the White Rock structure, having helped to expand the brand into Europe, believes Guernsey's PCC legislation has been adopted in some 40 jurisdictions worldwide with little variation.

"Other jurisdictions have changed the name in an attempt to differentiate, but effectively all 'PCC' legislation globally has been based on that originally formulated in Guernsey," says McLaughlin.

The structure's key feature is the legal ring-fencing of designated assets and liabilities it offers within the PCC so that each cell acts as a separate entity while sharing administrative efficiencies with the PCC core.

"The cell owner can concentrate on the business of the cell and the cell sponsor, for example Aon in the case of White Rock, manages the core," explains McLaughlin. It means the cell sponsor and the cell owner work in partnership and are perhaps more closely aligned than a traditional captive and insurance manager relationship. Speed of establishment is another positive of the PCC as the ability to establish cells quickly and to use them to provide insurance and risk financing solutions is a real tangible benefit to corporate worldwide.

In addition to White Rock, Guernsey's cell company expertise has been evidenced regularly since 1997. Some of the most notable examples include in 2010 with Heritage Insurance Management (now Artex Risk Solutions), achieving a worldwide first by amalgamating two PCCs – with 17 cells between them – into one. In the funds industry, Guernsey also hosted the first-ever conversion of a PCC to an incorporated cell company (ICC) during a process which created the world's largest ICC mutual fund.

Then there are the two ground-breaking longevity swap struc tures that were established in Guernsey in 2014, which used captive insurance companies in place of insurance intermediaries, thereby cutting out intermediary fees and removing the need for price averaging.

Record-breaking

The first of these saw the trustees of the BT Pension Scheme, Britain's largest corporate pension fund, set up its

own captive insurance company, and then reinsure its longevity risk with the US-based life insurance company, the Prudential Insurance Company of America. In the biggest ever deal of its kind, the arrangement covered 25% of the scheme's exposure to increased life expectancy and amounted to £16bn of the scheme's liabilities.

This was then followed by the Towers Watson 'Longevity Direct' structure, which enables pension schemes to gain direct access to the reinsurance market in order to hedge longevity risk for their defined benefit liabilities. Through a form of 'rent-a-captive' the structure allows pension schemes to own a ready-made insurance cell that can write insurance and reinsurance contracts for longevity swap transactions, particularly for those liabilities between £1bn and £3bn.

Both the BT and Towers Watson structures utilised a Guernsey ICC as the vehicle for their respective captive insurance companies, BTPS Insurance ICC Ltd and Towers Watson ICC Limited. Similarly, Artex Risk Solutions and PricewaterhouseCoopers (PwC) more recently joined forces to create the Guernsey-domiciled Iccaria Insurance ICC. Iccaria not only offers pension funds the benefit of cost-ef fective risk transfer, but also a flexible structure which enables pension funds to select the ser vice providers they wish to use to administer the arrangements.

Providing access to the reinsurance market through these types of cell structures is making the hedging of pension risk more affordable for schemes, while also reducing the complexity that is often associated with longevity hedging.

Beyond insurance

While initially introduced for use in Guernsey's captive insurance sector, Richard Sharp, Partner at Bedell Cristin, says the ability to also use cell companies in the funds sphere has only added to their appeal and innovativeness. Cell companies are often used as umbrella investment funds with each cell being used as an investment vehicle for different asset classes.

Sharp explains that asset classes can be segregated according to the risk profile while having the economy of a single company.

"A PCC fund will usually have a main scheme document that addresses matters that affect all the cells and the launch of individual cells can then be covered in shorter supplements covering matters specific to the particular cell. This means that the creation and licensing of new cells is easier and cheaper than creation of a new fund. This is particularly appealing to promoters looking to launch smaller investment vehicles," he said.

History and future

Steve Butterworth, director of insurance at the Guernsey Financial Services Commission until 2003, is the man widely credited with developing Guernsey's PCC concept.

He first had the idea for the concept when he was in the Cayman Islands back in around 1984, after learning that an association captive had run up large legal fees in its first year because every member was using independent counsel. This made Butterworth think about the need for assets to be segregated, but when he took the idea to the local authorities they were not so keen. It wasn't until he moved to Guernsey in 1986 that the idea would later be taken seriously, before coming to fruition in the mid-to-late 1990s.

He credits Nik van Leuven, then a private advocate, for drafting what he describes as an 'excellent piece of commercial legislation' that matched his own vision.

"I always thought that once the concept became internationally accepted, its use would become widespread across financial services and that has proven to be the case," said Butterworth recently.

"But I am still surprised at some of the areas it is not more widely used, including by institutions for mergers, acquisitions and disposals. It is an ideal piece of legislation for a banking group, especially to ring-fence assets and liabilities. As a result, there is still lots of development and diversification to come in the area of PCCs."

An original version of this article was first published by Captive Review's 2017 Cell & Series Guide.

WE ARE GUERNSEY is the brand under which Guernsey Finance promotes the island's financial services sector internationally. Guernsey Finance - the promotional agency for the island's finance industry internationally - is a joint industry and Government initiative responsible for the promotion of Guernsey. Under the leadership of Chief Executive Rupert Pleasant, the agency ensures that the core values and competencies of the island's finance sector are accepted and respected by the global community and that financial business development flows are enhanced.

PO Box 655, St Peter Port,
Guernsey, GY1 3PN
+44 (0)1481 720071
INFO@WEAREGUERNSEY.COM