

SCHEDULE 2

[SCHEDULE 12 TO THE 1994 REGULATIONS]

PART I

EXCESS EXPOSURE: METHOD OF CALCULATION

1. Unless the context requires otherwise, words and expressions contained in this Schedule bear the same meaning as in Parts VIII and IX of these Regulations.

2. For the purposes of this Schedule—

“business amount” means—

- (a) for a company carrying on only general business, the general business amount;
- (b) for a company carrying on only long term business, the long term business amount;
- (c) for a company carrying on both general business and long term business, in the case of its general business assets, the general business amount and in the case of its long term business assets, the long term business amount.

“connected company” of any company means—

- (a) that company’s holding company;
- (b) a subsidiary of that company;
- (c) a subsidiary of the holding company of that company.

“counterparty” in relation to a company means—

- (a) any one individual;
- (b) any one unincorporated body of persons;
- (c) any one company not being a member of a group;
- (d) any group of companies excluding any companies within the group which are dependants of the insurance company; or
- (e) any government of a state together with all the public bodies, local authorities or nationalised industries of that state,

in which the insurance company has made investments or against whom it has rights whether in pursuance of a contract entered into by the insurance company or otherwise; and reference to dealings with or by a counterparty includes dealings with or by any person or body of persons included within the definition of counterparty;

“counterparty exposure” shall be determined in accordance with paragraph 13 below;

“debts due or to become due” includes any debts which would become due if the insurance company were to exercise any right to which it is entitled to require payment or repayment of the same;

“diversified contract for differences” means a contract for differences whose value does not depend to a significant extent on fluctuations in the value of, or income from, assets or any of the descriptions in paragraphs 1 to 9, 11 or 13 to 19 of Part II of this Schedule and “undiversified contract for differences” shall be construed accordingly;

“excess concentration with a number of counterparties” shall be determined in accordance with paragraph 17 below;

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“general business amount” means the aggregate of the company’s insurance liabilities (net of reinsurance) in respect of general business and an amount equal to whichever is the greater of 400,000 units of account or 20 per cent. of the general premium income;

“group” has the meaning given in section 262 of the Companies Act 1985;

“hybrid security” means a debt security, other than an approved security, the terms of which provide, or have the effect that, or contain an option which if exercised by the issuer would have the effect that the holder does not or would not have an unconditional entitlement to payment of interest and repayment of capital in full within seventy five years of the relevant date;

“index linked liabilities” means contractual liabilities to policyholders to pay index linked benefits;

“insurance liabilities” means amounts calculated in accordance with Part IX of these Regulations in respect of those items shown at C and D under the heading “Liabilities” set out in paragraph 9 of Schedule 9A to the Companies Act 1985;

“long term business amount” means the amount of the company’s insurance liabilities (net of reinsurance ceded and excluding property linked liabilities), together with—

- (a) the amount of the required margin of solvency (or the amount of the minimum guarantee fund if greater) determined in accordance with regulations 18 to 22 above (or, in the case of a company whose head office is not in the United Kingdom, the amount which would apply if its head office were in the United Kingdom) less the amount of any implicit item valued in accordance with regulations 24 to 26 of these Regulations; and
- (b) the amount of any deposit-back in connection with a contract of reinsurance in respect of long-term business,

save that for the purposes of assessing compliance with the permitted asset exposure limit, it shall further exclude index linked liabilities.

“permitted asset exposure limit” has the meaning set out in paragraph 3 of this Schedule;

“permitted counterparty exposure limit” has the meaning set out in paragraph 4 of this Schedule;

“property linked liabilities” means contractual liabilities to policyholders in respect of property linked benefits;

“readily realisable” in relation to a listed investment means a listed investment to which regulation 51(3) either does not apply or applies by reason only that—

- (a) the listing of the investment has been temporarily suspended following receipt of price sensitive information by the stock exchange on which the investment is listed or the regulated market on which facilities for dealing have been granted; or
- (b) the extent of the holding would prevent an orderly disposal of the investment for not more than 97½ per cent of the market value;

“short term deposit” means a sum of money which may be withdrawn at the discretion of the lender without penalty or loss of accrued interest by giving notice of withdrawal of one month or less.

3. The permitted asset exposure limit for assets of any of the descriptions in any paragraph of Part II of this Schedule is the percentage of the business amount set out immediately below that paragraph. In the case of an asset which is not covered by any of the descriptions in Part II of this Schedule (other than a derivative contract) the permitted asset exposure limit is nil.

4. The permitted counterparty exposure limit is—

- (a) where the counterparty is an individual or an unincorporated body of persons, 5 per cent of the business amount;

- (b) where the counterparty is a counterparty of the type mentioned in sub-paragraph (d) in the definition of counterparty, 5 per cent of the business amount;
- (c) where the counterparty is a body corporate or group, each of—
 - (i) 20 per cent of the business amount;
 - (ii) 10 per cent of the business amount where the exposure arises other than by reason that debts are due or to become due as a result of short term deposits made with an approved credit institution;
 - (iii) 5 per cent of the business amount where the exposure is other than to bodies which are approved counterparties.

Calculation of exposure to assets

5. A value shall be ascribed to assets of each description which shall be an amount determined in accordance with the provisions of Part VIII of these Regulations, or where the assets are of a description for the valuation of which no provision is made in Part VIII of these Regulations, an amount which would reasonably be paid by way of consideration for an immediate assignment or transfer of such assets. The amount by which the company is exposed to assets of each description shall be determined by adjusting the value of the assets in accordance with paragraphs 6 to 11 below.

Adjustments in respect of futures contracts

6. The figure arrived at under paragraph 5 above in respect of assets of each description shall be increased or decreased by the value of assets of that description which the company is deemed to have acquired or disposed of pursuant to a futures contract.

7. For the purposes of paragraph 6 above, the company shall be deemed to have acquired or disposed of assets pursuant to a futures contract if, at the relevant date, it has entered into (and not closed out) a futures contract which—

- (a) provides for the acquisition of assets by that company; or
- (b) is listed and provides for the disposal of assets by the company or
- (c) is not listed but provides for the disposal of assets by the company to an approved counterparty within one year of the relevant date.

Adjustments in respect of options

8. The figure arrived at under paragraphs 5 to 7 above in respect of assets of each description shall be increased or decreased by the value of assets of that description which the company is deemed to have acquired or disposed of pursuant to an option.

9. For the purposes of paragraph 8 above, the company shall be deemed to have acquired or disposed of assets pursuant to an option if, at the relevant date, it is a party to an option and it is prudent to assume that the option will be exercised and the option is one which—

- (a) provides for the acquisition of assets by the company; or
- (b) is listed and provides for the disposal of assets by the company; or
- (c) is not listed but provides for the disposal of assets by the company to an approved counterparty within one year of the relevant date.

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Adjustments in respect of an undiversified contract for differences or a contract or asset having the effect of a derivative contract

10. The amount arrived at in accordance with paragraphs 6 to 9 above shall be increased or decreased by an amount representing the value of assets which the company is deemed to have acquired or disposed of under—

- (a) an undiversified contract for differences; or
- (b) a contract or asset other than a diversified contract for differences which has the effect of a derivative contract.

11. For the purposes of paragraph 10 above, the company shall be deemed to have achieved the effect of such contract by entering into appropriate futures contracts or options. The assets deemed to be acquired or disposed of shall be dealt with in accordance with the provisions in paragraphs 6 and 8 respectively.

Excess asset exposure

12. The amount by which the company is exposed to assets of a particular description in excess of the permitted asset exposure limit shall be calculated by subtracting the permitted asset exposure limit for assets of that description from the corresponding amount of the exposure, calculated in accordance with paragraphs 5 to 11 above. For this purpose, exposure to assets shall be excluded to the extent that such exposure has caused the recognition of excess exposure to assets of a different description. If the figure arrived at is negative, it shall be taken to be zero.

Calculation of exposure to a counterparty

13. Subject to paragraphs 14 and 15 below, the value of all investments (determined in accordance with regulation 51 above) issued by any one counterparty and the value of all rights (determined in accordance with regulations 48, 55 and 56 above) against that counterparty, in each case up to the amount of the appropriate permitted asset exposure limit, shall be aggregated. Where the counterparty is an issuer of a collective investment scheme falling within paragraph (c) of regulation 52 above, the value of units or other beneficial interest in the collective investment scheme shall be included.

14. Where an insurance company has rights in respect of an obligation to be fulfilled by a counterparty and the obligation is a secured obligation secured by:—

- (a) cash deposited with, or a letter of credit established with, or securities issued by, or a guarantee provided by, an approved credit institution or an approved financial institution;
- (b) approved securities; or
- (c) listed securities to which regulation 51(2)(a) applies which have been deposited with an approved credit institution or an approved financial institution and which in either case will not be available for the benefit of creditors generally in the event of the winding-up of the counterparty,

the aggregation required by paragraph 13 above need not include the value of such rights.

15. If the insurance company has liabilities to the counterparty which may be offset against the above-mentioned assets in accordance with generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate for insurance companies, then such liabilities may be offset for the purposes of the aggregation required by paragraph 13 above.

Excess counterparty exposure

16. The amount by which the company is exposed to a counterparty in excess of the permitted counterparty exposure limit shall be calculated by subtracting from the amount of the exposure to such counterparty the amount of the permitted counterparty exposure for such counterparty. If the figure arrived at is negative, it shall be taken to be zero. If the company is exposed to a counterparty in excess of the permitted counterparty exposure limit in more than one of the circumstances set out in sub-paragraph (c) of paragraph 4 above, it shall only be required to make deductions in respect of the circumstances leading to the greatest excess exposure.

Excess concentration with a number of counterparties

17. Where there is exposure to a counterparty of the type mentioned in paragraph 4(c)(ii) above which exceeds 5 per cent. of the business amount, 40 per cent. of the business amount shall be deducted from the aggregate of such exposures (each of which, for this purpose, shall be taken not to exceed 10 per cent. of the business amount). The amount so arrived at shall be the excess exposure to a number of counterparties. Where this amount is negative it shall be taken to be zero.