
STATUTORY INSTRUMENTS

1994 No. 1981

The Friendly Societies (Insurance Business) Regulations 1994

PART II

MARGINS OF SOLVENCY

Application: Part II

3.—(1) This Part of these Regulations applies to a society to which section 48 of the 1992 Act applies.

(2) Subject to regulation 62 below, a society which is—

- (a) an incorporated friendly society, or
- (b) an authorised registered friendly society,

is prescribed for the purposes of section 48(1)(c) of the 1992 Act.

Required margin of solvency

4.—(1) The margin of solvency of a society is the excess of the value of its assets over the amount of its liabilities determined in accordance with Parts IV and V of these Regulations.

(2) Subject to paragraphs (3) to (5) below, the margin of solvency to be maintained by a society to which this Part of these Regulations applies pursuant to section 48 of the 1992 Act (referred to in these Regulations as “the required margin of solvency”) shall be determined—

- (a) with respect to a society which carries on long term business, in accordance with Schedule 1; and
- (b) with respect to a society which carries on general business, by taking the greater of the two sums resulting from the application of the two methods of calculation set out in Schedules 2 and 3 respectively.

(3) For a contract to which section 117(4) of the 1992 Act applies, the required margin of solvency shall be determined by taking the aggregate of the results arrived at by applying—

- (a) in the case of so much of the contract as is within any class of long term business, the appropriate method prescribed by Schedule 1 for that class; and
- (b) in the case of so much of the contract as is within general business class 1 or 2, the method of calculation set out in Schedule 2 (excluding paragraphs 7, 8 and 9).

(4) Where a society carries on long term business and owing to the nature of that business more than one margin of solvency is produced in respect of that business by the operation of this Part of these Regulations, the margins in question shall be aggregated as regards the society in order to arrive at its required margin of solvency for long term business.

(5) Where a society carries on both long term and general business and is accordingly required to maintain separate margins of solvency in respect of the two kinds of business—

- (a) these Regulations shall apply for determining the margin of solvency for each kind of business separately; and
- (b) assets other than those representing the funds maintained by the society in respect of its long term business, if they are not included among the assets covering the liabilities and the margin of solvency relating to the society's general business, may be included among the assets taken into account in covering the liabilities and the margin of solvency for the society's long term business.

Guarantee fund and minimum guarantee fund

5.—(1) Subject to paragraphs (2) and (3) below, one-third of a required margin of solvency (being, in the case of long term business, the required margin of solvency determined in accordance with regulation 4(4) above) shall constitute the amount (“the guarantee fund”) prescribed for the purposes of section 49(1) of the 1992 Act.

(2) In the case of a society which is—

- (a) an incorporated friendly society; or
- (b) a registered friendly society to which section 37(2) or (3) of the 1992 Act applies, the guarantee fund shall not be less than an amount (“the minimum guarantee fund”) arrived at in accordance with regulation 6 for long term business and regulation 7 for general business respectively.

(3) In the case of long term business, items that are not implicit items must be at least large enough to cover either the minimum guarantee fund or 50 per cent. of the guarantee fund, whichever is the greater.

Minimum guarantee fund: long term business

6.—(1) In the financial year during which a society is first authorised under section 32 of the 1992 Act to carry on long term business, the minimum guarantee fund shall be the amount in column 2 of the table below, which corresponds to the society's annual contribution income in respect of that business in the last preceding financial year, as shown in column 1 of the table

Contribution Income (in ECU)	Minimum Guarantee Fund (in ECU)
1,000,000 or less	100,000
1,000,001-1,500,000	200,000
1,500,001-2,000,000	300,000
2,000,001-2,500,000	400,000
2,500,001-3,000,000	500,000
3,000,001 or more	600,000

but where a society had no annual contribution income in respect of long term business in the last preceding financial year or has not been in existence long enough to have a preceding financial year, the minimum guarantee fund shall be an amount of 100,000 ECU.

(2) In any subsequent financial year during which a society continues to be authorised to carry on long term business, the minimum guarantee fund shall be the greater of either—

- (a) the amount in column 2 of the table in paragraph (1) above that corresponds to the society's annual contribution income in respect of long term business in the last preceding financial year; or

- (b) the amount of the minimum guarantee fund required to be maintained by the society in the last preceding financial year,

providing that if the amount referred to in subparagraphs (a) and (b) above is the same, the minimum guarantee fund shall be that amount.

(3) Where a society obtains authorisation under section 32 of the 1992 Act to carry on long term business—

- (a) of a class additional to that in respect of which it is already authorised; or
- (b) in a part of the United Kingdom additional to that in respect of which it is already authorised,

a minimum guarantee fund of 600,000 ECU shall be maintained by that society for the whole of its long term business (that is to say, not only for the additional business carried on but also for the business previously carried on).

Minimum guarantee fund: general business

7. The minimum guarantee fund in respect of general business carried on by a society shall be an amount of 225,000 ECU.

Valuation of solvency margins

8.—(1) Where a society to which this Part of these Regulations applies has assets in excess of its liabilities, then, in addition to any other applicable valuation regulations in Part IV of these Regulations, paragraphs (2) and (3) below shall have effect for determining the extent to which the value of the assets exceeds the amount of liabilities in connection with the required margin of solvency, the guarantee fund and the minimum guarantee fund.

(2) In the case of a society carrying on general business, any claim which the society has against its members by way of a call for supplementary contributions for a financial year shall have its full value for that financial year, subject to the limitation that the value shall not exceed—

- (a) 50 per cent. of the difference between the maximum contributions and the contributions called in, or
- (b) 50 per cent. of the required margin of solvency.

(3) The items mentioned in regulations 9 to 11 below (which relate to future surpluses, zillmerising and hidden reserves and shall be known as “implicit items”) shall have no value, except with the consent of the Commission given upon application of a society. Where the Commission so consents—

- (a) any of the implicit items may be valued in accordance with the provisions of regulations 9 to 11 with respect to long term business; and
- (b) the implicit item relating to hidden reserves may be valued in accordance with regulation 11 with respect to general business.

Implicit items: future surpluses

9.—(1) The implicit item relating to future surpluses may be valued at not more than 50 per cent. of the full amount of future surpluses.

(2) For the purposes of paragraph (1) above, the full amount of future surpluses shall be obtained by multiplying the estimated annual surplus by a factor which shall as nearly as may be represent the average number of years remaining to run on policies, but shall, if it exceeds 10, be reduced to 10.

(3) For the purposes of paragraph (2) above—

- (a) the estimated annual surplus shall be taken to be one-fifth of the surplus (“the periodic surplus”) made in long term business over a period of five years (“the relevant period”) ending on the last day of the most recent completed financial year during which a valuation for the purposes of section 46 of the 1992 Act or regulation 11 of the 1987 Regulations has been carried out, substantial items of an exceptional nature being excluded, and
- (b) the average number of years remaining to run on policies shall be calculated—
 - (i) by multiplying the number of years to run on each policy by the actuarial value of the benefits payable under the policy, adding together the products so obtained and dividing the total by the aggregate of the actuarial values of the benefits payable under all the policies; or
 - (ii) by an approximation to this method of calculation suitable to the circumstances of the case, including, where appropriate, an approximation involving the grouping of contracts,
 appropriate allowance being made in either case for premature termination of contracts.
- (4) For the purposes of paragraph (3)(a) above—
 - (a) where a valuation under section 46 of the 1992 Act or regulation 11 of the 1987 Regulations has been carried out annually in relation to the relevant period, the annual surplus made in long term business for any particular year of the relevant period shall be taken to be the surplus (if any) arising in the long term business funds since the last such valuation, and the periodic surplus shall be taken to be the aggregate of those annual surpluses less any deficiencies in the long term business funds during that period;
 - (b) where a society has carried on long term business throughout the relevant period but valuations under section 46 of the 1992 Act or regulation 11 of the 1987 Regulations have not been made annually in that period, the periodic surplus shall be taken to be the aggregate of surpluses arising in the long term business funds since the last valuation preceding the relevant period less any deficiencies in the long term business funds since the last valuation, except that the surplus or deficiency arising in the period ending with the first valuation within the relevant period shall be proportionately reduced to allow for any period of time falling outside the relevant period;
 - (c) where a society has not carried on long term business throughout the relevant period, the periodic surplus shall be taken to be the aggregate of any surpluses arising in the long term business funds during that part of the relevant period for which long term business was carried on less any deficiencies in the long term business funds during that part of that period.

Implicit items: zillmerising

10.—(1) Where zillmerising (as defined in paragraph (7) below) is appropriate but either is not practised or is at a rate less than the loading for acquisition costs included in the premium then, subject to paragraph (6) below, the implicit item relating to zillmerising may be valued at an amount not exceeding the difference between—

- (a) the non-zillmerised or partially zillmerised figure for mathematical reserves maintained by the society concerned; and
- (b) a figure for mathematical reserves (determined in accordance with Part V of these Regulations) zillmerised at a rate equal to the loading for acquisition costs included or allowed for in the premium.

(2) Where zillmerising is not practised, then subject to paragraph (6) below, the value given by paragraph (1) above (less any amount relating to temporary assurances) shall not exceed 3.5 per cent. of the aggregate of the difference between—

- (a) the relevant capital sums for long term business activities; and
- (b) the mathematical reserves (excluding mathematical reserves for temporary assurances).

(3) Where zillmerising is practised but is at a rate less than the loading for acquisition costs, then, subject to paragraph (6) below, the value given by paragraph (1) above (less any amount relating to temporary assurances) together with the difference between the partially zillmerised mathematical reserves and the non-zillmerised mathematical reserves shall not exceed 3.5 per cent. of the aggregate of the difference between—

- (a) the relevant capital sums of long term business activities; and
- (b) the mathematical reserves (excluding mathematical reserves for temporary assurances).

(4) In paragraphs (2) and (3) above “relevant capital sums” means—

- (a) for whole life assurances, the sum assured;
- (b) for policies where a sum is payable on maturity (including policies where a sum is also payable on earlier death), the sum payable on maturity;
- (c) for deferred annuities, the capitalised value of the annuity at the vesting date (or the cash option if it is greater);
- (d) for capital redemption contracts, the sums payable at the end of the contract period; and
- (e) for linked long term contracts, notwithstanding subparagraphs (a) to (d) above, the lesser of—

- (i) the amount for the time being payable on death, and
- (ii) the aggregate of the value for the time being of the units allocated to the contract (or, where entitlement is not denoted by means of units, the value for the time being of any other measure of entitlement under the contract equivalent to units) and the total amount of the premiums remaining to be paid during such part of the term of the contract as is appropriate for zillmerising, or, if such premiums are payable beyond the age of seventy-five, until that age,

excluding in all cases any vested reversionary bonus and any capital sums for temporary assurances.

(5) Where, under the contract relating to any such business as is mentioned in paragraph (4) above, the payment of premiums is to stop before the sum assured becomes due, then, notwithstanding the said paragraph (4), “relevant capital sums” in paragraphs (1) to (3) above shall be taken to mean the mathematical reserves appropriate for that contract at the end of the premium-paying term.

(6) For the purposes of this regulation—

- (a) reserves for vested reversionary bonuses shall not be regarded as mathematical reserves, and
- (b) the result given by paragraph (1), (2) or (3) above shall be reduced by the amount of any undepreciated acquisition costs brought into account as an asset.

(7) “Zillmerising” means the method known by that name for modifying the net premium reserve method of valuing a long term policy by increasing the part of the future premiums for which credit is taken so as to allow for initial expenses.

Implicit items: hidden reserves

11. The implicit item relating to hidden reserves, if it consists of hidden reserves resulting from the underestimation of assets and overestimation of liabilities (other than mathematical reserves), may, in so far as the hidden reserves in question are not of an exceptional nature, be given its full value.