



Getting to grips with Part VII transfers

In this article, Kate Angell and Richard Bulmer explore how Part VII transfers can be used as an effective tool for the management and restructuring of insurance business.

Insurance business transfers have been permitted in the UK for a number of years, originally under the regime set out in Schedule 2C of the Insurance Companies Act 1982 and currently under Part VII of the Financial Services and Markets Act 2000. Regimes also exist for the transfer of both direct and reinsurance business across Europe under the Third Non Life Insurance Directive (which was implemented in 1994) and the EU Reinsurance Directive (which was implemented in 2007), although these Directives only prescribe minimum standards. As a result, the procedures in place for effecting insurance business transfers vary between countries.

Insurance business transfers, or Part VII transfers as they are commonly known in the UK, enable the complete transfer of business from one insurer to another, with no contractual liability remaining with the original insurer. They are accomplished without the permission of the policyholders and without any voting mechanism required, although Court sanction of the transfer is required in the UK, and policyholders (and other parties such as the FSA) have the right to be heard by the Court. Part VII transfers also require an 'Independent Expert' to be appointed. The Independent Expert is required to consider the effect of the proposed transfer on each of the groups of policyholders who may be impacted, and to produce a report setting out his/her opinion. When forming his opinion, the Independent Expert needs to consider the effect of the transfer on both the security of policyholders' contractual rights and the levels of service provided to

policyholders. The Independent Expert's report is relied on by the Court and also made available to policyholders and the FSA.

Historically, there have been around 15 non-life Part VII transfers each year, with the profile of such transfers increasing recently with the Part VII transfer of the insurance business of Lloyd's Names for 1992 and prior years of account from Equitas to a company within the Berkshire Hathaway group. In this article, we consider some of the reasons for effecting such transfers and recent developments in the area.

Part VII transfers are a useful tool for insurance companies and are carried out for a variety of reasons. We explore below some of the most common reasons:

- **Achieving finality** – Part VII transfers are often undertaken to achieve true finality for the transferor company, for example, for the Lloyd's Names in the recent Equitas transfer. Reinsurance does not achieve this finality – with the reinsured always maintaining exposure to the underlying business. After a Part VII transfer has been completed, the transferor has no remaining exposure to the transferred business, while at the same time cover for policyholders is maintained.
- **Cost savings and capital releases** – many Part VII transfers are effected between companies within the same group so that companies can be deregulated and wound up, resulting in both cost savings (for example, via a reduction in both management time and administration costs) and capital releases.
- **Mergers and acquisitions** – Part VII transfers are effected in connection with mergers and acquisitions for a number of reasons. For example, to transfer similar portfolios of business into one entity to be sold (or to enable a sale of the remaining business to progress) or as an alternative way of acquiring a portfolio (or a combination of portfolios at the same time) rather than purchasing the entire company.
- **Schemes of arrangement** – Part VII transfers are also used in preparation for a scheme of arrangement. For example, where the insurance company currently contains business which cannot be included in a scheme of arrangement, such as compulsory insurance policies (for example, employers' liability insurance). This business can be removed from the company via a Part VII transfer prior to effecting a scheme of arrangement.
- **Restructuring overseas business** – Part VII transfers are also effected in order to restructure overseas business. For example, companies have transferred portfolios of business written through a European branch of a UK insurance company to a (sometimes newly established) insurance company in the European country instead. Another example is where companies have transferred a portfolio of business written through a UK branch of a non-EU insurance company to an EU insurance company, for example, to take advantage of passporting rights in Europe.

Figure 1 | Historical Part VII transfers

<p>Internal restructuring</p>	<p>Within the RSA group, inwards reinsurance was previously written across 16 subsidiary companies. A transfer was effected to move all of this business into another subsidiary company, British Engine Insurance Limited. The aim of the transfer was to simplify the administration of the inwards reinsurance business of RSA and to help facilitate an exit from this business, should an appropriate opportunity arise.</p> <p>A transfer was effected of the business within Munich Re America's remaining UK branch, which was in run-off, to Great Lakes (also part of the Munich Re group) to allow the UK branch to be closed.</p> <p>The business of several Zurich operations was transferred into a single company, the UK Branch of Zurich Insurance Ireland Limited, to improve capital efficiency and to simplify the structure in Europe, with the aim of improving operational efficiency and risk management capabilities.</p>
<p>Restructuring overseas business</p>	<p>RSA combined all of its current Irish operations into its existing local insurance company, Europa General Insurance Company Limited, which has now been renamed as RSA Insurance Ireland Limited.</p>
<p>Achieving finality for the insurer, without terminating policyholders' cover</p>	<p>The transfer of the insurance business of Lloyd's Names for 1992 and prior years of account from Equitas to Equitas Insurance Limited, another subsidiary in the Equitas Group of companies.</p>
<p>Separating out long-tail casualty exposures from core operations</p>	<p>In 2007, discontinued London market business with exposure to North American asbestos and environmental liabilities was transferred from St. Paul Travelers Insurance Company Limited to Unionamerica Insurance Company Limited (which was then a fellow group company). Unionamerica was subsequently sold off in December 2008.</p>
<p>Combining multiple subsidiaries</p>	<p>Following the merger of Nissan Fire & Marine and Yasuda Fire & Marine in 2002 to form Sompo Japan Insurance, the European subsidiary of Nissan (NICEL) went into run-off while the Yasuda European subsidiary continued to write business (including renewals from NICEL). A Part VII transfer was then carried out in 2007 to combine the two European subsidiaries.</p>
<p>Restructuring between countries</p>	<p>A transfer was effected of the treaty reinsurance business of SCOR UK to the UK branch of SCOR Global P&C SE following the integration of Revios and Converium into the SCOR group. The transfer formed part of the restructuring of SCOR SE as a hub company with six geographical divisions.</p>
<p>Transfers involving Lloyds syndicates</p>	<p>Syndicates 37 and 2037 historically provided capital to the Highway motor insurance business. The transfer of these syndicates' business into the Highway Insurance Company Limited enabled Highway to exit from Lloyd's. The aim of the transfer was to simplify the group structure, accounting and regulatory processes and to streamline their capital position.</p>
<p>Transfer of compulsory insurances in preparation for a solvent scheme of arrangement</p>	<p>Minster, The Contingency and Malvern insurance companies transferred their compulsory insurances to Groupama in 2008 in advance of proposing a solvent scheme of arrangement.</p>



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Figure 1 sets out some historical Part VII transfers to illustrate some of the reasons for effecting such transfers.

Since the first insurance business transfers in the UK were sanctioned, the process by which such transfers are effected has evolved and changed over time. Some of these changes have been gradual in nature while others have been more sudden, such as the changes to the Financial Services & Markets Act 2000 (FSMA) last year. We consider some of the recent changes below:

■ **Amendments to the**

FSMA – three amendments were made which came into force on 30 June 2008. These amendments were:

- Power to transfer reinsurance protections – to put beyond all doubt that accompanying reinsurance and other contracts, which are related to the main business being transferred, may be transferred as part of a Part VII transfer.
- Notification of reinsurers – an additional requirement to give notice of the transfer application to all reinsurers whose contracts of reinsurance are proposed to be transferred as part of the Part VII process, in the same way that policyholders need to be notified. This requirement is to a large extent simply the extension of what was typically already regarded as good practice.

- Lloyd's Names – the final amendment removed the restriction on the ability of certain former names of Lloyd's to transfer their insurance business, enabling the Equitas Part VII transfer to proceed.

■ **The FSA's involvement** – the FSA now levies fees for Part VII transfers (currently £10,000 for non-life transfers) and issues two reports to the Court: the first in advance of the Directions Hearing (when the Court considers the proposed transfer and the plans for publicising it), and a further report in advance of the Final Hearing (when the proposed transfer is sanctioned by the Court). Previously, only one report was provided by the FSA in advance of the Final Hearing, and prior to that the FSA did not produce any reports at all. The purpose of the FSA's reports is to provide the Court with information on the FSA's views in relation to the proposed Part VII transfer, in particular, the basis on which the FSA does or does not object to the proposed transfer going ahead.

■ **Supplementary reports** – all Part VII transfers require a report from an Independent Expert, and there has been a gradual trend for supplementary reports to be produced for the final Court hearing. These have generally been produced for one of two reasons: to respond directly to an

objection which has been raised, or to consider the effects of events subsequent to the original report. The latter of these has become more relevant where significant changes to the economy have occurred during the period since the original report was produced, or the companies involved have published new financial information. The Independent Expert considers whether changes subsequent to the original report affect the conclusions and opinions reached.

Conclusion

While the process surrounding Part VII transfers has developed and evolved over time (and we expect it will continue to do so), such transfers remain an effective and useful tool for the management of insurance business.

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