

Amendments to the Insolvency Arrangements for Insurers: Consultation

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General Comments

We generally support the proposals outlined in the consultation and the suggestions made therein seem sensible. There are already separate rules for insurers and developing those in the way specified is not as controversial as creating a new separate regime for a particular type of debtor.

We do have some concerns about the multi-stage approach that is being adopted i.e. making some changes now and for this to be followed by further related changes later. Instead, it may be better to hold off and make all of the desired changes at the same time, in order to produce a more coherent and less piecemeal regime. It is also difficult to comment on a lot of what is proposed in the consultation in the absence of detail regarding how these proposals will appear in legislative form. As such, our comments are subject to that caveat.

Responses to Questions

We respond to the specific consultation questions as follows.

General Questions

1. In what circumstances do you envisage these proposals would be used?

We can foresee that the proposals would be used in relation to insolvent insurers and financially distressed but pre-insolvent insurers. We note that the proposed test for the court exercising its powers aligns with that for administration and that the court's consideration of the most likely alternative is reminiscent of the requirement for Part 26 and Part 26A schemes and plans (under the Companies Act 2006), and is also similar to what is done in the context of challenges to CVAs. Due to familiarity and alignment with the current law, we can see the advantage of using existing tests. However, given the combination of tests in the proposals, as compared with the tests for other processes which may be easier to meet, it is not entirely clear to us when exactly these proposals would be used instead of other processes. We are also not sure that it is entirely clear as to the precise point at which this process would become available.

2. Do you envisage any impediments to the use of the proposed measures in practice?

Given that the existing procedure has not been used, there is a danger that the proposed measures will not be used for similar reasons (whatever those might be). It is possible that a lack of knowledge about the proposed measures or a lack of familiarity with them, and the fact that there are no examples of the existing process having been used would act as impediments. Bringing greater clarity to the law and publicising the proposals appropriately may, however, make them more likely to be used in practice.

3. Do you agree that these proposals would usefully add to the flexibility with which the distress of an insurer could be managed?

They give a further option to deal with a distressed insurer and this of course adds to the flexibility, provided that it is viable to use the procedure.

4. Do you have any other comments on these proposals or the current insolvency arrangements for insurers?

We have nothing to add beyond our general comments above, particularly the issues with considering the law here separately from a broader review.

Proposal One:

- 5. How will the proposed amendments to section 377 FSMA enhance the UK authorities' ability to manage the distress of an insurer, resulting in a better outcome for policyholders and creditors?**

They provide another option. The fact that they give an option at an earlier, pre-insolvency, stage presumably does enhance the ability to manage the distress of an insurer, and ought to result in a better outcome for policyholders and creditors (as a whole).

- 6. To what extent do you believe that the proposed amendments to section 377 FSMA will improve the usability of the write-down procedure?**

Increasing clarity and certainty in relation to the procedure will improve its usability. The provision of more detail regarding its operation will encourage others to use it, as currently this may be a major issue causing it not to be used. Expanding the scope of when the procedure can be used also logically makes it more likely that the procedure will be used and the publicity involved in making the amendments will also alert others to the fact that this procedure is available.

- 7. Do you believe the tests which the court would need to be satisfied are met in order to sanction a write-down under section 377 FSMA (as amended by this proposal) are sufficient to safeguard against undue impact of a write-down on an insurer's creditors (including its policyholders)?**

By aligning the tests with those for administration, the point at which the procedure can be used is pushed back before insolvency arises, which may impact on creditors, but with a view to achieving a better outcome for them. Using the test that the court must be satisfied that the write-down would be reasonably likely to lead to a better outcome for the insurer's creditors as a whole is not, however, without its issues, as different groups of creditors may have different interests and there may be debate about what is meant by the interests of creditors as a whole. The combination of tests should in theory safeguard the interests of creditors but it may be difficult to administer the combination. It is also more convoluted than some other processes.

Given that this is a procedure relating to one type of business, there may not be a large number of cases involving this procedure, and so it could be a considerable period of time before there is useful body of case law to anticipate how courts will deal with relevant issues. However, the fact that existing tests are being used does mean that case law for e.g. administration and Part 26/26A schemes and plans can be helpfully used.

- 8. Do you support the nominee write-down manager being able to provide independent views to the court (including on the impact of the write-down on an insurer's creditors (including its policyholders)) at a write-down court hearing?**

Yes, this seems sensible. It is consistent with the roles of parties in other processes e.g. nominees in CVAs and monitors in the new moratorium (introduced by the Corporate Insolvency and Governance Act 2020).

- 9. Would the proposed amendments to section 377 FSMA be likely to impact an insurer's costs (including in relation to debt issuance)?**

We are not able to comment on this.

10. To what extent would the proposed moratorium on legal process during a write-down under section 377 FSMA assist in the writedown process?

It would logically seem that the proposed moratorium would assist the process by reducing the uncertainty and difficulties in assessing the insurer's estate that might arise otherwise. We agree with the reasons set out in the consultation paper. Some assistance might be gleaned by considering the moratorium provisions introduced under the Corporate Insolvency and Governance Act 2020, e.g. in relation to how they operate and how they have been used so far.

11. Do you have any other comments on Proposal One?

Having a write-down without the creditors' consent, particularly pre-insolvency, perhaps feels counter-intuitive. The fact that there is the possibility of a subsequent write up is, however, an important qualification of this. Consideration should be given as to whether there ought to be creditor input in the process, since there could be a considerable change to the debts due to them. In relation to the absence of involvement of creditors, we wonder why the proposal has been constructed in a different way to alternative options that do involve creditors. It may be because the procedure is an outgrowth of an option that has so far just been available to the court and is not a self-standing procedure. Nevertheless, we can see some merit here in not involving creditors as there may be a large number of policyholders in particular and administering creditor involvement would be very difficult in practice. We simply suggest that consideration be given to the issue of creditor involvement and wonder whether the rationale of the current proposals in this respect could perhaps be communicated more clearly.

Proposal Two:

12. Do you support the introduction of a write-down manager to support a write-down under section 377 FSMA (as amended by Proposal One)?

Yes. This makes sense, particularly in the expanded version contemplated. And see our answer to question number 8 above regarding equivalent parties in other processes. Given the technical issues involved, it is desirable to have an expert carrying out the function of write-down manager in an official capacity.

13. To what extent do you agree with the proposed eligibility criteria for a write-down manager under Proposal Two?

These all seem fine to us. More clarity on what is meant by "a suitably qualified insurance professional" would be useful. A decision needs to be made as to whether a court would have some discretion about this and ultimately have to make a determination or whether it will be objectively outlined in legislation.

14. Do you think the proposed role and powers of the write-down manager would be adequate to ensure the development/implementation of a write-down is in the interests of the insurer and its creditors (in particular policyholders)?

The powers seem to be sensible and obvious ones. It is useful that the court is able to vary them, dependent on the circumstances.

15. Do you have any other comments on Proposal Two?

We note as per para B.91 that there is to be no requirement for a bond, which we agree with, but we wonder whether it should be a requirement that there is appropriate professional indemnity cover in place.

A manager has to be independent but balance the interests of different parties, so it is a difficult role. It is important that it is possible to challenge the actions of the manager but the court needs to recognise the difficulty of the position and there will inevitably need to be an element of discretion on the part of the manager.

Proposal Three:

- 16. Do you agree that the proposed moratorium under Proposal Three would help provide stability, leading to better outcomes for policyholders and creditors overall, in the circumstances outlined above?**

Logically, and similar to our answer to 10 above, it will provide stability and certainty and allow for the efficient operation of the procedure, which should lead to better outcomes for policyholders and creditors overall.

- 17. How would the proposed moratorium under Proposal Three affect the terms on which insurers are able to enter into financial contracts and service contracts?**

It is difficult to discern what effect it would have on the terms on which insurers are able to enter into financial contracts and service contracts. It may be the case that such contractual counterparties would require a greater degree of financial and solvency information about an insurer compared to other types of business, which may feed through into different terms for contracts. However, this is merely speculation and we do not have particular evidence in this regard.

- 18. Factoring in the safeguards outlined above, do you have any concerns about the impact of the proposed moratorium under Proposal Three on the rights of an insurer's counterparties?**

Having safeguards and the ability to get a moratorium lifted in appropriate circumstances are crucial. Again, there may be lessons or information arising from the 2020 Act provisions that could be helpfully used here. Consideration may also be given to whether the differences in relation to the regime for insurers, in comparison to other types of debtor, are justified by the fact of the debtor being an insurer.

- 19. Do you have any other comments on Proposal Three?**

No.

Proposal Four:

- 20. Do you agree that the proposed stay under Proposal Four would help provide stability, leading to better outcomes for policyholders and creditors overall, in the circumstances outlined above?**

We can see the logic of this, as a temporary measure at least. It would stave off what would be the insurance equivalent of a run on the bank. It is a lot more difficult to manage the situation and the procedure in the interests of the creditors as a whole if parties can choose to cash in, and where it is not known when they might do this and how much will have to be paid out. The stay consequently provides more certainty.

- 21. Factoring in the safeguards outlined above, do you have any concerns about the impact of the proposed stay under Proposal Four on the rights of an insurer's policyholders?**

The ability to apply for an exemption from the stay is important. Constructing a provision to give effect to what is proposed in para B.164 will be difficult. For instance, at what point will there be considered to be too many exemptions and once this is decided what happens to existing exemptions granted? Attention may also need to be given to e.g. whether the stay will automatically suspend the running of any contractual time limits regarding when the policy can be cashed in, although we do recognise that a party who would be affected could always apply for an exemption in such a case.

- 22. Do you have any other comments on Proposal Four?**

No.

Proposal Five:

23. To what extent do you agree with government's proposal to ensure protected policyholders are not financially worse off as a result of a write down under section 377 FSMA (as amended by Proposal One), as compared to insolvency?

We think this makes sense. It is not desirable to incentivise insolvency processes in comparison to write down. Parties should not be worse off as a result of write down compared to insolvency. The potential for protected policyholders to be financially worse off should be taken into account at the stage when the court is considering the alternative to a write down. The proposal is better aligned with the relevant test and there is reduced complexity – e.g. the different level of recovery under FSCS in write down and then in an insolvency process can be rather difficult to compare. We support the rationale for the change proposed here that is outlined at para B.169.

24. Do you have any other comments on Proposal Five?

No.