
STATUTORY INSTRUMENTS

1987 No. 2132

The Friendly Societies (Long Term Insurance Business) Regulations 1987

PART III

REGULATION OF AUTHORISED SOCIETIES

Solvency Provisions

Annual actuarial investigation

11.—(1) Every authorised society shall, once in every period of twelve months, cause an investigation to be made into its financial condition in respect of its long term insurance business by a qualified actuary appointed by the society.

(2) Where a society has branches, the investigation shall be made into the financial condition of the branches together with the central body.

(3) The actuary's investigation shall include—

- (a) a valuation of the liabilities of the society attributable to its long term business, and
- (b) a determination of any excess over those liabilities of the assets representing the fund or funds maintained by the society in respect of that business, and, where any rights of any long term policy holders to participate in a surplus relate to any particular parts of such a fund, a determination of any excess of assets over liabilities in respect of each of those parts.

(4) For the purposes of the determination required by paragraph (3)(b) above, the value of any assets shall be determined in accordance with Part VI, and the amount of any liabilities shall be determined in accordance with Part VII, of these Regulations.

(5) When such an actuarial investigation has been made a valuation report shall be made to the Chief Registrar, in such form and containing such particulars as the Chief Registrar may prescribe in the exercise of his powers under the 1974 Act as extended by regulation 60 below.

(6) Three copies of the valuation report required by paragraph (5) above shall be sent to the Chief Registrar within six months after the close of the period to which the report relates; but if in any case it is made to appear to the Chief Registrar that the circumstances are such that a longer period than six months should be allowed, the Chief Registrar may extend that period by such period not exceeding three months as he thinks fit.

(7) The provisions of paragraph (6) above (as to the number of copies to be sent to the Chief Registrar, the period allowed for that purpose, and the power of the Chief Registrar to extend that period) shall, notwithstanding the provisions of section 43(1) (Annual return) of the 1974 Act, also apply in relation to the annual returns required from societies by that provision.

Required margin of solvency

12.—(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 Part VI and Part VII of these Regulations.

(2) Every authorised society shall maintain a margin of solvency (hereinafter referred to as “the required margin of solvency”) which shall be determined in accordance with the provisions of regulations 13 to 17 below.

Long term classes I and II

13.—(1) For long term business of class I or II the required margin of solvency shall be determined by taking the aggregate of the results arrived at by applying the calculation described in paragraph (2) below (“the first calculation”) and the calculation described in paragraphs (3), (4) and (5) below (“the second calculation”).

(2) For the first calculation—

- (a) there shall be taken a sum equal to 4 per cent of the mathematical reserves without any deduction for reinsurance cessions;
- (b) the amount of the mathematical reserves at the end of the last preceding year of account after the deduction of reinsurance cessions shall be expressed as a percentage of the amount of those mathematical reserves before any such deduction; and
- (c) the sum mentioned in sub-paragraph (a) above shall be multiplied—
 - (i) where the percentage arrived at under sub-paragraph (b) above is greater than 85 per cent, by that greater percentage, and
 - (ii) in any other case, by 85 per cent.

(3) For the second calculation—

- (a) there shall be taken, subject to paragraphs (4) and (5) below, a sum equal to 0.3 per cent of the capital at risk for contracts on which the capital at risk is not a negative figure;
- (b) the amount of the capital at risk at the end of the last preceding year of account for contracts on which the capital at risk is not a negative figure, after the deduction of reinsurance cessions, shall be expressed as a percentage of the amount of that capital at risk before any such deduction; and
- (c) the sum arrived at under sub-paragraph (a) above shall be multiplied—
 - (i) where the percentage arrived at under sub-paragraph (b) above is greater than 50 per cent, by that greater percentage, and
 - (ii) in any other case, by 50 per cent.

(4) Where a contract provides for benefits payable only on death within a specified period and is valid for a period of not more than three years from the date when the contract was first made, the percentage to be taken for the purposes of paragraph (3)(a) above shall be 0.1 per cent; and where the period of validity from that date is more than three years but not more than five years, the percentage to be so taken shall be 0.15 per cent.

(5) For the purposes of paragraph (4) above, the period of validity of the contract evidencing a group policy is the period from the date when the premium rates under the contract were last reviewed for which the premium rates are guaranteed.

(6) For the purposes of the second calculation, the capital at risk is—

- (a) in any case in which an amount is payable in consequence of death other than a case falling within sub-paragraph (b) below, the amount payable on death, and

(b) in any case in which the benefit under the contract in question consists of the making, in consequence of death, of the payment of an annuity, payment of a sum by instalments or any other kind of periodic payments, the present value of that benefit, less in either case the mathematical reserves in respect of the relevant contracts.

(7) When the amount of the mathematical reserves referred to in paragraph (2)(a) above, or the amount of the capital at risk referred to in paragraph (3)(a) above, is to be calculated for the purposes of determining the required margin of solvency, the day as on which that amount is calculated shall be the same as that on which the margin of solvency is determined; and the mathematical reserves referred to in paragraph (6) above shall also be calculated as on that day when the capital at risk in question is that referred to in paragraph (3)(a) above, but shall be calculated as at the end of the last preceding year of account when the capital at risk in question is that referred to in paragraph (3) (b) above.

Long term classes III and VII

14.—(1) For long term business of class III or VII the required margin of solvency shall be determined in accordance with paragraphs (2) to (5) below.

(2) In so far as a society bears an investment risk, the first calculation shall be applied.

(3) In so far as—

- (a) a society bears no investment risk, and
- (b) the total expired and unexpired term of the relevant contract exceeds five years, and
- (c) the allocation to cover management expenses in the relevant contract has a fixed upper limit which is effective as a limit for a period exceeding five years,

the first calculation shall be applied, but as if regulation 13(2)(a) above contained a reference to 1 per cent instead of 4 per cent.

(4) If neither paragraph (2) nor paragraph (3) above applies, then, subject to paragraph (5) below, the required margin of solvency is zero.

(5) Where a society covers a death risk, a sum arrived at by applying the second calculation disregarding regulation 13(4) and (5) shall be added to any required margin of solvency, including a required margin of solvency of zero, arrived at under paragraph (2), (3) or (4) above.

Long term classes IV and VI

15. For long term business of class IV or VI the required margin of solvency shall be determined by applying the first calculation.

Long term class V

16. For long term business of class V the required margin of solvency shall be equal to 1 per cent of the assets of the relevant tontine.

Supplementary business

17. For a contract which contains supplementary business, the required margin of solvency shall be determined by taking the aggregate of the results arrived at—

- (a) in the case of so much of the contract as is within a class of long term business, by applying the appropriate method prescribed for that class in regulation 13, 14, 15 or 16 above, and
- (b) in the case of so much of the contract as is supplementary business, by applying the method of calculation set out in Schedule 3.

Aggregation where more than one margin of solvency

18. Where the nature of the society’s long term business is such that 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.

Guarantee fund and minimum guarantee fund

19.—(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 the provisions of regulations 13 to 17 above and arrived at, where applicable, in accordance with regulation 18 above) shall constitute the amount (“the guarantee fund”) prescribed for the purposes of regulation 31 below.

(2) The guarantee fund shall not be less than an amount (“the minimum guarantee fund”) arrived at in accordance with regulation 20 below.

(3) Items that are not implicit items within the meaning of regulation 21(3) below 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

20.—(1) In the year of account during which it is first authorised, a society shall maintain a minimum guarantee fund consisting of the amount in column 2 of the table below, which corresponds to its annual contribution income in the last preceding year of account, as shown in column 1 of the table.

Contribution Income (in units of account)	Minimum Guarantee Fund (in units of account)
500,001—1,000,000	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—3,500,000	600,000

(2) Where the amount of the minimum guarantee fund determined under paragraph (1) above is below the full minimum guarantee fund of 600,000 units of account, that amount shall be increased by a tranche of 100,000 units of account in the year following any year of account during which the society’s contribution income has increased by 500,000 units of account until the full minimum guarantee fund has been reached.

(3) Where the amount of a society’s minimum guarantee fund has been increased in accordance with paragraph (2) above, the increased amount shall be maintained thereafter, notwithstanding any later fall in the society’s annual contribution income.

(4) Where a society seeks to be authorised to carry on long term business of a kind additional to that which it is already authorised to carry on, it shall, if it obtains authorisation for the additional business, maintain the full minimum guarantee fund of 600,000 units of account for the whole of its business (that is to say, not only for the additional business carried on but also for the business previously carried on).

Valuation of solvency margins

21.—(1) Where a society has assets equal to or in excess of its liabilities, 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) The required margin of solvency shall consist of the assets of the society, including in particular—

- (a) free reserves not corresponding to underwriting liabilities, and
- (b) any carry forward of surplus,

less any intangible items.

(3) The items mentioned in regulations 22 to 24 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 Chief Registrar given upon the application of a society. Where the Chief Registrar so consents, any of the implicit items may be valued in accordance with the terms of his consent and the provisions of the said regulations 22 to 24.

Implicit items: future surpluses

22.—(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 made in long term business over a period of five years ("the relevant period") ending on the last day of the most recent year of account during which a valuation for the purposes of regulation 11 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.

Implicit items: zillmerising

23.—(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 (not less than those required by Part VII 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 sub-paragraphs (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.
- (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

24. 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.

Matching and localisation

Matching

25.—(1) Where the liabilities of an authorised society in any particular currency exceed 5 per cent of the society's total liabilities, then subject to paragraphs (2) and (3) below, the society shall hold sufficient assets expressed in or capable of being realised without exchange risk into that currency to cover at least 80 per cent of the society's liabilities in that currency.

(2) In so far as the liabilities for property linked benefits are covered by assets which determine the benefits payable under a linked long term contract, paragraph (1) above shall not apply.

(3) In so far as the liabilities for property linked benefits are determined by reference to assets expressed in or capable of being realised without exchange risk into a currency other than the currency in which the society's obligations to its member are expressed, those liabilities shall for the purposes of paragraph (1) be deemed to be liabilities in the first-mentioned currency.

(4) For the purposes of paragraphs (1) and (3) above, an asset is capable of being realised without exchange risk into a currency if it is reasonably capable of being realised into that currency without risk that changes in exchange rates would reduce the cover of liabilities in that currency.

(5) In this regulation—

“assets”, except in the case of assets of the kind referred to in regulation 26 below, means assets valued in accordance with Part VI of these Regulations;

“liabilities” means provision by a society to cover liabilities arising under or in connection with contracts of insurance (not being liabilities relating to insurance business excluded by regulation 27 below).

“property linked benefits” has the meaning given by regulation 34(1) below.

Localisation

26.—(1) Assets held pursuant to regulation 25 above shall be held—

- (a) if they cover liabilities in sterling, in the United Kingdom;
- (b) if they cover liabilities in any other currency, in the United Kingdom or in the country of that currency.

(2) For the purposes of applying paragraph (1) above to tangible assets and assets consisting of a claim against a debtor or a listed or unlisted investment, the following provisions shall have effect—

- (a) a tangible asset shall be regarded as held in the place where it is situated;
- (b) an asset consisting of a claim against a debtor shall be regarded as held in any place where it can be enforced by legal action;
- (c) an asset consisting of a listed investment shall be regarded as held in any place where—
 - (i) there is a recognised United Kingdom stock exchange or a stock exchange of repute outside the United Kingdom where it is listed, or

- (ii) there is a securities market outside the United Kingdom, being a market of repute in which prices of all securities in which there are dealings are publicly listed and which is supervised by a public body, where it is dealt in;
- (d) an asset consisting of an unlisted investment issued by an incorporated company shall be regarded as held in the place where the head office of that company is situated.

Exclusion

27. Nothing in regulation 25 or 26 shall apply to insurance business carried on outside the United Kingdom.

Partial transfers

Transfer of part of long term business

28.—(1) Subject to the following provisions of this regulation, an authorised society (“the transferor”) may transfer part of its long term business to another authorised society (“the transferee”).

(2) The proposed transfer shall be approved by special resolution, within the meaning of section 86 (Meaning and registration of special resolutions) of the 1974 Act, in respect of both the transferor and the transferee.

(3) In respect of the transferor, at the general meeting at which the special resolution was passed, the proposed transfer shall further be approved by a resolution passed by not less than three-quarters of those members to whose contracts with, or benefits due from, the society the transfer relates, who either vote in person or by proxy at the meeting.

(4) The transferor shall give information relating to the terms of the proposed transfer to its members—

- (a) by sending to each member, not less than fourteen days before the date of the general meeting at which the special resolution for the transfer is to be proposed, a notice in terms to be approved by the Chief Registrar; or
- (b) if the Chief Registrar so allows in the case of all or any of the members of the society, by placing an advertisement, in terms approved for the purpose by him, in such newspaper or newspapers, and at such time or times, as he may specify.

(5) The transferee shall produce to the Chief Registrar a statement by a qualified actuary that the transferee will possess the margin of solvency required by law after the proposed transfer has taken place.

(6) A transfer of business under the provisions of the Regulation shall not prejudice any right of a creditor of the transferor or the transferee.

(7) A partial transfer under this regulation shall be deemed to be a transfer under section 82 (Amalgamation and transfer of engagements) of the 1974 Act for the purposes of the Chief Registrar’s powers under that provision and of the Industrial Assurance Commissioner’s powers under section 36 (Transfers from one society or company to another) of the 1923 Act.

Investment

Investments of authorised societies

29. Section 46 (Investment of funds) of the 1974 Act shall, from the date on which a society is authorised under regulation 5 or 6 above, have effect in relation to that society as though the words in subsection (1) from “or any part thereof” to the end of that subsection were deleted.