

**EXPLANATORY MEMORANDUM TO THE
INSURERS (REORGANISATION AND WINDING-UP) (LLOYD'S)
REGULATIONS 2005**

2005 No. 1998

1. This Explanatory Memorandum has been prepared by Her Majesty's Treasury and is laid before Parliament by command of Her Majesty.

2. Description

2.1 The Insurers (Reorganisation and Winding-Up) (Lloyd's) Regulations will implement EU Directive 2001/17/EC on the reorganisation and winding-up of insurance undertakings, in relation to the Lloyd's of London market.

2.2 The purpose of these Regulations is to apply the same conditions regarding reorganisation measures and winding-up procedures to the 'association of underwriters known as Lloyd's'¹ as have already been put in place for all other UK insurers through the Insurers (Reorganisation and Winding-Up) Regulations 2004.

3. Matters of special interest to the Joint Committee on Statutory Instruments

None.

4. Legislative Background

4.1 HM Treasury are using their powers under section 2(2) of the European Communities' Act 1972 to implement into domestic legislation in the United Kingdom the Insurers (Reorganisation and Winding-Up) Directive² in respect of the Lloyd's of London market.

4.2 The Insurers (Reorganisation and Winding Up) Regulations 2003 (SI 2003/1102) implemented that Directive into UK law for all UK insurers except Lloyd's, due to Lloyd's unique structure that did not prove compatible with the provisions of the Regulations without further complex adaptation and refinement. These Regulations came into force on 17 April 2003.

4.3 The Insurers (Reorganisation and Winding-Up) Regulations 2004³ (S! 2004/353) replaced the 2003 Regulations principally in order to give effect to changes to the administration provisions of the Insolvency Act 1986 brought in by the Enterprise Act

¹ This term is used to refer to the regulated undertaking within the context of Community law; it otherwise has no legal personality.

² Directive 2001/17/EC of the European Parliament and of the Council of 19 March 2001 on the reorganisation and winding-up of insurance undertakings, OJ L 110 of 20 April 2001, p. 28

³ http://www.opsi.gov.uk/cgi-bin/htm_hl.pl?DB=opsi&STEMMER=en&WORDS=insur+reorganis+wind+regul+2004+&COLOUR=Red&STYLE=s&URL=http://www.opsi.gov.uk/si/si2004/20040353.htm#muscat_highlighter_first_match

2002, and which were commenced in September 2003. These are referred to as “the principal Regulations”.

4.4 The Insurers (Reorganisation and Winding Up) (Amendment) Regulations 2004 (SI 2004/546) made some minor amendments to the 2004 Regulations

4.5 This statutory instrument makes necessary adaptations to the principal Regulations in order to implement the obligations of the Directive with regard to the association of underwriters known as Lloyd’s.

4.6 These Regulations will be subject to negative resolution by Parliament.

4.7 The Transposition Note is attached.

5. Extent

5.1 This instrument applies to the whole of the United Kingdom. (Services in channel Islands and IOM are not subject to community law).

6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy Background

7.1 The purpose of the Directive is to establish rules on the adoption of reorganisation measures⁴ and winding-up procedures⁵ for insurance undertakings (as defined by the First Life and the First Non-Life Directives⁶) across the EU, for the proper functioning of the internal market and the protection of creditors.

7.2 Reorganisation and winding-up are different processes and the requirements for each are different. The Directive requires coordination rules for both reorganisation measures and winding-up proceedings, as well as rules governing the priority, which different types of creditor have in respect of the assets of an undertaking in the event

⁴ For the purposes of the Directive, “reorganisation measures” are defined as measures “involving any intervention by administrative bodies or judicial authorities which are intended to preserve or restore the financial situation of an insurance undertaking and which affect the pre-existing rights of parties other than the insurance undertaking itself; including, but not limited to, measures involving the possibility of a suspension of payments, suspension of enforcement measures or a reduction in claims”

⁵ For the purposes of the Directive, ‘winding-up proceedings’ are defined as “collective proceedings involving realising assets of an insurance undertaking and distributing the proceeds among the creditors, shareholders or members as appropriate, which necessarily involve any intervention by the administrative or the judicial authorities of a Member State, including where the collective proceedings are terminated by a composition or other analogous measure, whether or not they are founded on insolvency or are voluntary or compulsory”.

⁶ Directive 79/267/EEC and Directive 73/239/EEC. Directive 79/267 has now been replaced by the consolidating Life Assurance Directive 2002/83/EC.

of a winding-up. In particular, the Directive establishes that direct insurance claims should generally have precedence over other claims.

7.3 The prime objective of the Directive is to ensure that reorganisation measures or winding-up proceedings affecting an insurer are recognised in all Member States without further formality. Only the competent authorities (in the UK context, this would be the Courts, or the FSA) in the Member State in which an insurer is authorised (the insurer's "home Member State") can authorise the adoption of reorganisation measures or the opening of winding-up proceedings in respect of that insurer, including branches of that insurer in other Member States.

7.4 The First Life and the First Non-life Directives recognise the association of underwriters known as Lloyd's as an existing insurance undertaking in the UK for the purposes of those and later insurance directives. That association does not have any legal personality within the United Kingdom and thus in order to apply the obligations within the Reorganization and Winding-up Directive to the regulated entity it is necessary to apply its provisions to the members of Lloyd's who enter into insurance contracts as Lloyd's and are responsible on a several basis for meeting the liabilities under such policies as they have each written.

7.5 These Regulations identify the circumstances in which the powers and functions within them become exercisable, by establishing a 'trigger' for the Regulations to bite, in the event that the Lloyd's insurance market as a whole does not, or appears unlikely to, meet the solvency requirement set by the FSA. At this point, either the FSA or the Society of Lloyd's, or both, can apply to the Court for a Lloyd's Market Reorganisation Order, which would create the coordination mechanism within which the provisions of the Regulations could then operate.

7.6 This Order provides for the appointment of a reorganisation controller whose role it is to preserve or restore the financial situation of and confidence in the market, and to assist in achieving an outcome that is in the interests of creditors of members, and insurance creditors in particular. It will be for the reorganisation controller to ascertain the extent and have an overview of the difficulties and, in the light of this, to devise, in liaison with the FSA, a market reorganisation plan.

7.7 Priority will be given to insurance debts over all unsecured liabilities, and this attaches to the entire estate of insolvent members and former members, in line with the requirements of the Directive.

7.8 The Regulations also provide for:

- a moratorium on legal processes involving market participants and the Society, including all affected former members with continuing liabilities, who have not been specifically excluded from the Order;
- set-off arrangements for the liabilities and debtors of members at syndicate level;
- treatment of Premiums Trust Funds, Personal Reserves and Funds at Lloyd's as subject to rights in rem;

- treatment of policies reinsured to close as direct policies in the current year where the original policy was a direct policy.

7.9 HM Treasury undertook a thirteen-week consultation exercise and received nine broadly supportive responses to the proposals.

7.10 In light of the consultation responses, four amendments have been made to the Regulations, two in relation to the role of the reorganisation controller, one in relation to the time allowed for drawing up a reorganisation plan, and the final one to take account of differing insolvency provisions in Scotland.

7.11. More detailed analysis of the consultation responses can be found in the Final Regulatory Impact Assessment and the Feedback Statement.⁷

8. Impact

8.1 The impact of this instrument is primarily on the private sector, specifically the Lloyd's market.

8.2 Any impact on the public sector will rest principally with the FSA, which will be responsible for enforcing the provisions of this instrument, should the need arise.

8.3 The Final Regulatory Impact Assessment gives more detailed analysis of the wider impact of these Regulations.

9. Contact

All queries in relation to this instrument should be sent to Charlette Holt-Taylor at HM Treasury (Charlette.Holt-Taylor@hm-treasury.x.gsi.gov.uk).

⁷ Both of these will be published on the Treasury website: www.hm-treasury.gov.uk

**THE INSURERS REORGANISATION AND WINDING-UP DIRECTIVE
(2001/17/EC): A TRANSPOSITION NOTE IN RELATION TO LLOYD'S**

The Directive was implemented in the UK originally through Regulations (SI 1102/2003) made by HM Treasury. Those Regulations implemented the directive throughout the UK, except in relation to Lloyd's and made the necessary amendments to Scottish and Northern Ireland legislation. Those Regulations were replaced by further Regulations in 2004 (SI 2004/353) (referred to hereafter as the "principal Regulations") made by HM Treasury which adapted those original provisions to take into account the new UK provisions relating to administration of companies contained in Schedule B1 to the Insolvency Act 1986 and introduced by the Enterprise Act 2002. The Insurers (Reorganisation and Winding Up) (Lloyd's) Regulations 2005 ("the Lloyd's Regulations") to which this Note relates provide for the application of the principal Regulations in the case of Lloyd's. The original transposition note is also attached and should be read in conjunction with this one.

This note only describes the transposition of the main elements of the directive in relation to Lloyd's to the extent that special provisions for the Lloyd's market have been found to be necessary.

Article	Purpose	Implementation
Title I	Definitions	
2	Definition of insurance undertaking	Regulations 3, 4 and 5 describe the Lloyd's market reorganisation order, the conditions that have to be met before an application can be made and the objectives of the of the order. Regulation 13 provides for the application of the principal Regulations to members and former members of Lloyd's who are within the scope of a Lloyd's market reorganisation order
Title II	Reorganisation Measures	
5	Information to the supervisory authorities.	Regulation 9 of the principal Regulations as adapted by regulation 33 of the Lloyd's Regulations – this requires the court to inform the FSA (as the supervisory authority in the UK) of any decision to open reorganisation or winding-up proceedings. Regulation 10 as adapted by regulation 34 – requires the FSA, to inform the regulatory authorities in other Member States of any decision in the UK to open reorganisation or

		winding-up proceedings.
6	Publication	Regulation 11 as adapted by regulation 35 – requires publication in the <i>Official Journal of the European Communities</i> of summary information concerning a Lloyd's market reorganisation order and measures or proceedings in relation to particular members or former members of Lloyd's..
7	Information to known creditors – right to lodge claims	Existing UK law does not require claims to be formally lodged in order to receive payments. No action is, therefore, needed to implement this article of the Directive as it does not impact on existing legislation.
Title III	Winding-Up Proceedings	
8	Opening of winding-up proceedings – information to the supervisory authorities. (2) Winding-up measures shall be recognised throughout the Community without further formalities. (3) Supervisory authorities to be informed.	See Regulation 6(1) above. See Regulations 8 and 10 above.
9	Applicable law	Regulation 37 as adapted by regulation 46(4) implements this article by stating that winding-up proceedings within the UK will be conducted in accordance with the general law of insolvency of the UK.
10	Treatment of insurance claims	Part IV of the principal Regulations implements this article. These provisions have been adapted by regulations 40 and 43 of the Lloyd's Regulations. The Treasury is implementing the directive using Article 10's option (b) – insurance claims to have priority over all the assets of the insurer with the exception of preferential creditors

		<p>and creditors with claims on assets subject to rights in rem.</p> <p>Detailed adaptations are made in regulation 40 to allow for the provisions of the principal Regulations to be applied to members of Lloyd's of all descriptions. Regulation 41 of the Lloyd's Regulations provides that in relation to risks that are covered by a member under a reinsurance to close contract, if a debt would be treated as an insurance debt but for it being subject of a reinsurance to close contract it is to be regarded as an insurance debt of the member or members who at the time of the Lloyd's market reorganisation order have reinsured to close.</p>
14	Publication	See Regulation 11 above.
15	Information to known creditors	Regulation 12(1) as adapted by regulation 36 – requires all known creditors to be informed in writing as soon as reasonably practicable that winding-up proceedings have been commenced, together with other relevant information.
16	Right to lodge claims	Creditors, wherever domiciled already have a right to lodge claims under UK law. No further provision is necessary to implement this article.
17	<p>Languages and form</p> <p>Creditors may submit claims in an official language of the Member State in which they reside.</p>	Regulation 13 as adapted by regulation 37 implements this article.
18	Regular information to creditors	Regulation 14 as adapted by regulation 38 requires a liquidator to send a report to creditors once every twelve months. This does not prevent a court from providing for

		reports to be sent more frequently.
Title IV	Provisions common to reorganisation measures and winding-up proceedings	
19	Effects on certain contracts and rights	Articles 19 to 26 require no special adaptations
20	Third party rights in rem	
21	Reservation of title	
22	Set-off	
23	Regulated markets	
24	Detrimental acts	
25	Protection of third-party purchasers	
26	Lawsuits pending	