

Financial Security of Insurers & Related Issues

This note seeks to help our clients and prospective clients understand issues relating to the financial security of insurers. It provides general information only and each insurer must therefore be considered on their individual merits. Insurer ratings represent no guarantee but they are a guide to the likelihood of an insurer being able to meet its obligations.

We generally refer to ratings provided by the international rating agency Standard & Poor's (S&P). An S&P Insurer Financial Strength Rating is an opinion of the long term financial security of an insurer in respect of its ability to pay claims under its insurance policies. There are other rating agencies, such as AM Best and Moody's, who use similar methods of assessment but we are not a rating agency and provide no warranty or in any way validate the opinions or assessments of others.

Insurer ratings, regulatory arrangements and compensation schemes vary across the insurers we use. Should you wish to discuss any issues relating to the insurers we use, do not hesitate to talk to your usual Pound Gates contact.

Insurers rated 'BBB' or higher are regarded by S&P as having financial security characteristics that outweigh any vulnerabilities, and are likely to have the ability to meet financial commitments. An insurer holding one of the following four ratings is deemed to meet this criteria:

AAA

An insurer rated 'AAA' has extremely strong financial security characteristics. 'AAA' is the highest insurer financial strength rating assigned by S&P Global Ratings

AA

An insurer rated 'AA' has very strong financial security characteristics, differing only slightly from those rated higher.

A

An insurer rated 'A' has strong financial security characteristics, but is somewhat more likely to be affected by adverse business conditions than are insurers with higher ratings.

BBB

An insurer rated 'BBB' has good financial security characteristics, but is more likely to be affected by adverse business conditions than are higher rated insurers.

An insurer rated 'BB', 'B', 'CCC' and 'CC' is regarded by S&P as having vulnerable characteristics that may outweigh its strengths. 'BB' indicates the least degree of vulnerability within the range and 'CC' the highest.

BB

An insurer rated 'BB' has marginal financial security characteristics. Positive attributes exist, but adverse business conditions could lead to insufficient ability to meet financial commitments.

B

An insurer rated 'B' has weak financial security characteristics. Adverse business conditions will likely impair its ability to meet financial commitments.

CCC

An insurer rated 'CCC' has very weak financial security characteristics, and is dependent on favourable business conditions to meet financial commitments.

CC

An insurer rated 'CC' has extremely weak financial security characteristics and is likely not to meet some of its financial commitments.

SD or D

An insurer rated 'SD' or 'D' is in default on one or more of its insurance policy obligations but it is not under regulatory supervision that would involve a rating of 'R'.

R

An insurer rated 'R' is under regulatory supervision owing to its financial condition. The rating does not apply to insurers' subject only to non-financial actions such as market conduct violations.

NR

An insurer designated 'NR' is not rated, which implies no opinion about the insurer's financial security.

Ratings from 'AA' to 'CCC' may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.

A detailed explanation of S&P's ratings can be found on their website www.spglobal.com/ratings

Policyholder protection for UK customers - Insurer financial failure

If a UK insurer regulated by the Prudential Regulation Authority (PRA) cannot meet claims against it because it has been placed in liquidation (or provisional liquidation or administration) then eligible UK policyholders are entitled to compensation from the Financial Services Compensation Scheme (FSCS). The PRA and the Financial Conduct Authority (FCA) each make rules which sets out how FSCS cover works. The compensation is financed by a levy on the relevant firms.

Eligible policyholders are:

- Private individuals, sole traders and small businesses (including partnerships, unincorporated or mutual associations) with a turnover below £1,000,000.
- All policyholders in respect of compulsory insurances e.g. Third Party Motor Liability & Employers' Liability.

Compensation for PRA regulated firms (effective from 8 October 2020) is:

- 100% for compulsory insurance, professional indemnity insurance and/or claims arising from death or incapacity of the policyholder due to injury, sickness or infirmity.
- 90% for all other kinds of insurance.

Temporary Permissions Regime (TPR) and other non-UK authorised insurers

The TPR enabled EU / EEA firms that were passporting into the UK when the transition period ended on 31/12/2020 to continue operating temporarily in the UK, to insure UK risks.

A 3 year limit effective 01/01/2021 applies, during which time each insurer within it is expected to either;-

- apply to register a UK domiciled insurer; or
- give notice it will withdraw from the TPR regime.

If a TPR insurer wanted to continue operating and trading within the UK insurance market they were required to submit an application by 31/12/2022 (the sixth and final landing slot) to become fully authorised.

The FCA expect to determine most applications by the end of June 2023, although the exact timeframe for each application will depend on a number of factors. These include the firm's landing slot (i.e. when it applied) and the complexity and quality of the application. The TPR officially ends on 31/12/2023.

The FCA expect firms without a valid reason for not seeking full authorisation to voluntarily apply to cancel their temporary permission and either enter the Financial Services Contracts Regime (FSCR) to run-off their UK business (if eligible) or leave the UK regulatory perimeter.

Where firms fail to take either of these steps, the FCA are looking to take action and cancel their temporary permission.

Our Securities Committee have been closely monitoring the outcome of the application process for all identified TPR insurers within our agency portfolio and will continue to do so until TPR comes to an end on 31/12/2023.