Protected Cell Company (PCC)

An Introduction

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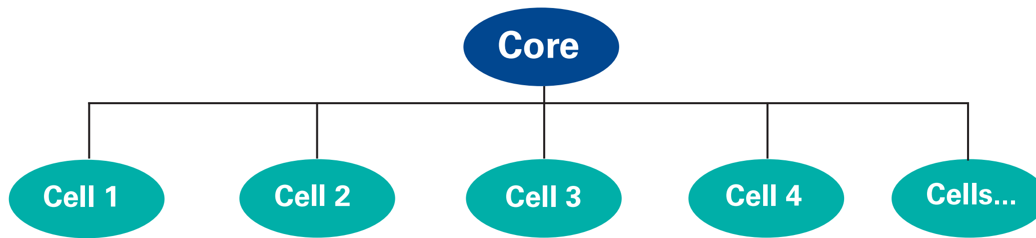
PCC Structure - Typical Structure



PCC Structure - Regulation

- A PCC is a type of company authorised in terms of:
  - the Insurance Business Act (Cap 403) ('the Act'); and
  - the Subsidiary Legislation 386.10 Companies Act (Cell Companies Carrying on Business of Insurance) Regulations, as amended by Legal Notice 391 of 2015.

- It is a single legal entity.

- There are two parts to the PCC namely, a non-cellular part (the Core) and protected cells (the cells).

- The number of cells is not limited.

- The cells created within the PCC can transact insurance/reinsurance business through the insurance/reinsurance licence held by the PCC.

- Despite the segregation of assets and liabilities that exists between the cells and the Core and among the cells themselves, a cell has no separate legal identity.

- The Core may or may not be authorised to write insurance and/or reinsurance business.

- A single Board of Directors takes responsibility for transactions within the Core and each of the cells, statutory and regulatory compliance and corporate governance requirements.

- The Core maintains and controls all the activities of the PCC.

- The Core has to maintain a minimum capital requirement at all times for regulatory purposes.

- The two most common types of PCC structures that currently exist are:
  - Type 1 : The Core does not write any insurance or reinsurance business.
  - Type 2 : The Core and the cells write insurance and/or reinsurance business. The cell shall write all or a subset of the classes of insurance business that the PCC is authorised to underwrite.

- For regulatory purposes:
  - The cellular assets of a cell will be primarily used to meet the liability of that cell;
  - The non-cellular assets (also known as the Core assets) can be utilised to meet the liability of the cell, only when the cellular assets of the cell have been exhausted and when there is recourse to the Core assets;
  - Cellular assets from other cells cannot be used to meet the liability of the cell.

Recourse Agreement

- Where there is recourse to the capital of the Core, this means that the Core capital can be transferred to the cell and can be used to meet the liabilities attributable of the cell.
- Any additional capital above the minimum capital can be transferred to the cells only where the cells of the PCC have recourse to the capital of the Core.
- Any recourse to the Core by the cell has to be clearly stated in the Cell Agreement.

Non-Recourse Agreement

- The law provides that where the cell exclusively carries on business of affiliated insurance or business of reinsurance (and provided that it is specifically permitted by the memorandum and articles of association of the PCC) there is no recourse to the assets of the Core.
- A non-recourse agreement effectively protects the Core from the creditors or the cells, otherwise a creditor can pursue the Core assets at the disadvantage of other cells that have recourse to the Core's assets.
- Where a cell exclusively carries on non-affiliated direct insurance business, non-recourse agreements may be permitted.
- Where there is no recourse to the capital of the Core, this means that no Core capital can be transferred to the cell and the cell has to be self-capitalised. The solvency ratio of the cell has to be at least 100% at all times.

PCC Structure - Commercial

- The PCC structures are generally used by:
    - Specialist run-off companies to ring-fence the portfolios bought or transferred; and
    - By companies who may want to "rent" a cell, for example, as a way of passporting into other European countries without setting up a company on the ground and having to put up the minimum capital requirement to meet the Solvency II capital requirements.

PCC Structure - Solvency II

- For Solvency II purposes, the PCC as a whole should have sufficient Eligible Own Funds to meet the Minimum Capital Requirement ("MCR") Absolute Floor which should be borne by the Core.

- The MCR Absolute Floor under Solvency II ranges from €1.2m up to €3.7m depending on whether the entity is an insurance and/or reinsurance company or captive.

- For PCCs, the notional Solvency Capital Requirement ("nSCR") has to be calculated for each cell as well as the Core, in the same manner as if they were all separate undertakings. This can be done using either the Standard Formula, Undertaking Specific Parameters (USPs) or an Internal Model (full or partial).

- Where multiple cells within the PCC structure exhibit similar characteristics, the calculation methodology applied to one cell may also be applied to any similar cell, provided the methodology produces sufficiently accurate results for all of the similar cells.

- The nSCR for each cell is determined by aggregating the capital requirements for each risk module and sub-module of the basic SCR using the procedure for aggregation of the standard formula prescribed by the Solvency II Directive. This means that diversification between the different risk modules and sub-module within a cell or a Core is permitted. No diversification is allowed between cells and/or between cells and the Core in the calculation.

- The SCR for the PCC as a whole, is the sum of the nSCR for each cell and the nSCR of the Core

$$SCR_{PCC} = nSCR_{Core} + nSCR_{Cell1} + nSCR_{Cell2} + \cdots + nSCR_{Celln}$$

- The Own Funds for each cell of the PCC are restricted as the assets over liabilities and subordinated liabilities within each cell cannot be transferred to cover all types of losses within the Core and any other cells.

- The Restricted Own Funds within a cell is determined as per the following two scenarios:

Scenario 1 – Restricted Own Funds greater than nSCR	Scenario 2 – Restricted Own Funds less than nSCR
Surplus of Own Funds in the cell	**Deficit in Own Funds in the cell**
Where the Restricted Own Funds of the cell are greater than the nSCR of the cell, then the Restricted Own Funds will be reduced to the nSCR in the calculation of the Total Own Funds of the PCC.	**Where the Restricted Own Funds of the cell are less than the nSCR of the cell, then the Restricted Own Funds for each cell will remain unadjusted and added to the Total Own Funds of the PCC when the cell has recourse to the capital of the Core.** **Where there is a non-recourse agreement (i.e. the cell cannot obtain capital from the Core), then the cell must have sufficient own funds to cover its nSCR at all times.**

Note:

- If the amount of the Restricted Own Funds within the cell are less than the nSCR, the PCC will only be in compliance with the SCR of the PCC as a whole when the Total Own Funds within the Core and the Restricted Own Funds within the cells combined are sufficient to cover that SCR.

SCR Calculation Example for the PCC

€ m	Core	Cell 1	Cell 2*	Cell 3**	PCC as a whole
nSCR	35	10	15	10	
SCR					70
AMCR	3.7				3.7
EOF	50	20	10	10	80
ROF		10	10	10	
Surplus/Deficit		10	(5)	0	10
Solvency Ratio	50/35 = 143%	10/10 = 100%	10/15 = 67%	10/10 = 100%	80/70 = 114%

Key:
SCR = Solvency Capital Requirement
nSCR = Notional SCR
EOF = Eligible Own Funds
ROF = Restricted Own Funds

Notes:
Assumption made:
*Cell 2 has recourse to Core assets and the deficit will be addressed through the use of Core assets
**Cell 3 has no recourse to Core assets and has to be self-capitalised at all times

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