Chapter 3

Cross sector groups

Guidance Notes for Classification of Groups

Classification of Groups (GENPRU 3.1.3 G) - This annex consists only of one or more forms. Forms are to be found through the following address. genpru_ch3_annex3G.pdf

Purpose and scope

The form is designed to identify groups and sub-groups that are likely to be financial conglomerates under the Financial Groups Directive. A group may be a financial conglomerate if it contains both insurance and banking/investment businesses and meets certain threshold tests. The *FCA* needs to identify conglomerates with their head offices in the EEA and those with their head offices outside the EEA, although this does not necessarily mean that the latter will be subject to EEA conglomerate supervision.

This form's purpose is to enable the *FCA* to obtain sufficient information so as to be able to determine how likely a group/sub-group is to be a financial conglomerate. In certain cases this can only be determined after consultation with the other EU relevant competent authorities. A second purpose of the form is therefore to identify any groups and sub-groups that may need such consultation so that this can be made as soon as possible. This should allow firms time to prepare to comply.

The third purpose of the form is to gain information from firms on the most efficient way to implement the threshold calculations in detail (consistently with the directive). We have, therefore, asked for some additional information in part 4 of the form.

A copy of this form can be found on the *FCA*'s Financial Groups Website with current contact details.

Please include workings showing the method employed to determine the percentages in part 2 (for the threshold conditions) and giving details of all important assumptions / approximations made in doing the calculations.

The definition of financial conglomerate includes not only conventional groups made up of parent-subsidiary relationships but groups linked by control and "consolidation Article 12(1) relationships". If this is the case for your group, please submit along with this form a statement that this is the case. Please include in that statement an explanation of how you have included group members not linked by capital ties in the questionnaire calculations.

A consolidation Article 12(1) relationship arises between undertakings in the circumstances set out in Article 12(1) of the Seventh Company Law Directive. These are set out in the Handbook Glossary (in the definition of consolidation Article 12(1) relationship). Broadly speaking, undertakings come within this definition if they do not form a conventional group but:

(a) are managed on a unified basis; or
(b) have common management.

General guidance

We would like this to be completed based on the most senior parent in the group, and, if applicable, for the company heading the most senior conglomerate group in the EEA. If appropriate, please also attach a list of all other likely conglomerate sub-groups.

Please use the most recent accounts for the top level company in the group together with the corresponding accounts for all subsidiaries and participations that are included in the consolidated accounts. Please indicate the names of any significant subsidiaries with a different year-end from the group's year-end.

Please note the following:

(a) Branches should be included as part of the parent entity.

(b) Include in the calculations overseas entities owned by the relevant group or sub-group.
(c) There are only two sectors for this purpose: banking/investment and insurance.
(d) You will need to assign non-regulated financial entities to one of these sectors:

- **banking/investment** activities are listed in – Annex 1 to the Capital Requirements Directive 2013/36/EU
- **insurance** activities are listed in - schedule 1 to, and *contracts of insurance* defined in article 3(1) of, the *Regulated Activities Order* .
- Any **operator of a UCITS scheme, insurance intermediary, mortgage broker and mixed financial holding company** does not fall into the directive definitions of either financial sector or insurance sector and should be treated for these purposes as being outside the financial sector. They should therefore be ignored for the purposes of these calculations.

Threshold tests

For the purpose of completing section 2 of the form relating to the threshold tests, the following guidance should be used. However, if you consider that for your group there is a more appropriate calculation then you may use this calculation so long as the method of computation is submitted with the form.

Calculating balance sheet totals

Generally, use total (gross) assets for the balance sheet total of a group/entity. However, investments in other entities that are part of the group will need to be deducted from the sector that has made the investment and the balance sheet total of the entity is added to the sector in which it operates.

Our expectation of how this may be achieved efficiently is as follows:

(i) Off-balance-sheet items should be excluded.
(ii) Where off-balance sheet treatment of **funds under management** and on-balance sheet treatment of **policy holders' funds** may distort the threshold calculation, groups should consult the *FCA* on the appropriateness of using other measures under article 3.5 of the Financial Groups Directive.
(iii) If consolidated accounts exist for a sub-group consisting of financial entities from only one of the two sectors, these consolidated accounts should be used to measure the balance-sheet total of the sub-group (i.e. total assets less investments in entities in the other sector). If consolidated accounts do not exist, intra-group balances should be netted out when calculating the balance sheet total of a single sector (but cross-sector intra-group balances should not be netted out).
(iv) Where consolidated accounts are used, minority interests should be excluded and goodwill should be included.
(v) Where accounting standards differ between entities, groups should consult the *FCA* if they believe this is likely materially to affect the threshold calculation.
(vi) Where there is a subsidiary or participation in the opposite sector from its parent (i.e. insurance sector for a banking/investment firm parent and vice versa), the balance sheet amount of the subsidiary or participation should be allocated to its sector using its individual accounts.
(vii) The balance-sheet total of the parent entity/sub-group is measured as total assets of the parent/sub-group less the book value of its subsidiaries or participations in the other sector (i.e. the value of the subsidiary or participation in the parent's consolidated accounts is deducted from the parent's consolidated assets).
(viii) The cross-sector subsidiaries or participations referred to above, valued according to their own accounts, are allocated pro-rata, according to the aggregated share owned by the parent/sub-group, to their own sector.
(ix) If the cross-sector entities above themselves own group entities in the first sector (i.e. that of the top parent/sub-group) these should (in accordance with the methods above) be excluded from the second sector and added to the first sector using individual accounts.

Solvency (capital adequacy) requirements

Generally, the solvency requirements should be according to sectoral rules of the *FCA* that would apply to the type of entity. However, you can use EEA rules or local rules in the circumstances set out in Part 6 of ■ GENPRU 3 Annex 1. But if this choice makes a significant difference, either with respect to whether the group is a financial conglomerate or with respect to which sector is the biggest, you should consult with the *FCA* . Non-regulated financial entities should have proxy requirements calculated on the basis of the most appropriate sector. If sub-groups submit single sector consolidated returns then the solvency requirement may be taken from those returns.

Our expectation of how this may be achieved efficiently is as follows:

(i) If you complete a solvency return for a sub-group consisting of financial entities from only one of the two sectors, the total solvency requirement for the sub-group should be used.
(ii) Solvency requirements taken must include any deductions from available capital so as to allow the appropriate aggregation of requirements.
(iii) Where there is a regulated subsidiary or participation in the opposite sector from its parent/sub-group, the solvency requirement of the subsidiary or participation should be from its individual regulatory return. If there is an identifiable contribution to the parent's solvency requirement in respect of the cross-sector subsidiary or participation, the parent's solvency requirement may be adjusted to exclude this.
(iv) Where there is an unregulated financial undertaking in the opposite sector from its parent/sub-group, the solvency requirement of the subsidiary or participation should be one of the following:
(a) as if the entity were regulated by the *FCA* under the appropriate sectoral rules;
(b) using EU minimum requirements for the appropriate sector; or
(c) using non-EU local requirements* for the appropriate sector.
Please note on the form which of these options you have used, according to the country and sector, and whether this is the same treatment as in your latest overall group solvency calculation.
(v) For banking/investment requirements, use the total amount of capital required.
(vi) For insurance requirements, use the total amount of capital required.

Market share measures

These are not defined by the directive. The aim is to identify any standard industry approaches to measuring market share in individual EU countries by sector, or any data sources which are commonly used as a proxy.

Article I.

Article II. Threshold tests

Test F2

B/S of banking/investment + insurance sector = result %

B/S total

Test F3/F4/F5

B/S of insurance sector

B/S of banking/investment sector + insurance sector = A%

B/S of banking/investment sector

B/S of banking/investment sector + insurance sector = B%

Solvency requirement of insurance sector

Solvency requirement of banking/investment sector +insurance sector = C%

Solvency requirement of banking/investment sector

Solvency requirement of banking/investment sector +insurance sector = D%

The relevant percentage for the insurance sector is:

(A% + C%)/2 = I %

The relevant percentage for the banking/investment sector is:

$(B\% + D\%)/2 = BI\ \%$

The smallest sector is the sector with the smallest relevant percentage.

Article III. If $I\% < BI\%$ then F3 is insurance, $F4 = A\%$, and $F5 = C\%$

Article IV. If $BI\% < I\%$ then F3 is banking/investment, $F4 = B\%$ and $F5 = D\%$