IRA

Insurance Regulatory Authority

IRA/PG/17

GUIDELINE TO THE INSURANCE INDUSTRY ON INSURANCE RISK

MAY 2013

To: All Insurance & Reinsurance Companies

GUIDELINE ON INSURANCE RISK FOR INSURERS

This guideline on insurance risk is issued pursuant to section 3A of the Insurance Act for observance by Insurance and Reinsurance Companies.

The guideline aims at ensuring that insurance companies are managed in a sound and prudent manner by having effective risk management systems for identifying, assessing and mitigating risks inherent in the insurer's core business processes.

The insurer's risk management framework must provide reasonable assurance that its core business risks are prudently managed.

To this end, the Insurance Regulatory Authority issues this guideline on insurance risk to be effective from 30th June, 2013.

SAMMY M. MAKOVE
COMMISSIONER OF INSURANCE & CHIEF EXECUTIVE OFFICER

THE INSURANCE ACT (CAP 487)

IRA/PG/17

GUIDELINE TO THE INSURANCE INDUSTRY ON INSURANCE RISK

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1.0 AUTHORIZATION

IN EXERCISE of the powers conferred by sections 3A (a), (b) and (g) of the Insurance Act, the Insurance Regulatory Authority (herein referred to as Authority) issues the Guideline set out here below, for observance by all insurance companies registered under the Insurance Act Cap 487, in order to offer guidance on principles to be adhered to in product design, pricing, underwriting, claims management, reserving and reinsurance.

2.0 INTRODUCTION

2.1 This guideline establishes a set of principles for identifying, assessing and mitigating risks involved in the insurance business processes.

2.2 The core business activities of insurance companies that expose the insurer to insurance risks include: reinsurance, reserving, underwriting, claims management, product design and pricing.

3.0 KEY REQUIREMENTS

The requirements of this guideline are:

3.1 The Authority shall require the insurer to establish and operate within effective systems of risk management and internal controls.

3.2 The insurer shall be required to set up a risk management system that considers the nature, scale and complexity of its business processes.

3.3 The insurer shall be required to have appropriate written policies that are approved by the Board for their core business processes i.e. for reinsurance, reserving, underwriting, claims management, product design and pricing.

3.4 It is ultimately the responsibility of the Board and Senior Management to ensure that the risk management system is designed and operated to identify, assess, monitor, manage and report on all reasonably foreseeable material risks of an insurer in a timely manner.

3.5 The insurer shall avail all information required by the Authority in regards to risk management and internal controls.

4.0 GENERAL PRINCIPLES

4.1 The insurer shall develop risk policies in a way to help the employees understand their responsibilities.

4.2 The insurer shall be required to hold internal regular communication and training on risk policies.

4.3 The insurer's Board shall be required to carry out its responsibilities for risk oversight.

4.4 In addition, the insurers shall apply the guideline issued by the Authority in regard to Risk Management and Internal Controls.

5.0 INSURANCE RISK

5.1 The insurer shall be exposed to insurance risk if it has inadequate or inappropriate reinsurance, reserving, underwriting, claims management, product design and pricing which will lead to financial loss and the consequent inability to meet its liabilities.

5.2 The insurer's risk management system must provide reasonable assurance that the insurance risk is being prudently managed, having regard to factors such as the size, business mix and complexity of the insurer's operations.

5.3 The insurer shall be required to develop policies on product design, pricing, underwriting, claims management, reserving and reinsurance.

6.0 PRODUCT DESIGN

6.1 Product design involves the introduction of a new insurance product into the market or enhancement of an existing insurance product.

6.2 To minimize the risks in regard to product design, the insurer shall ensure that it develops the following for all its insurance products:

i. a business case supporting the need for the products;

ii. funding strategy for new and repackaged products

iii. an implementation plan for channeling the products into the market

iv. methods of monitoring compliance with the products design and policies

v. a risk register incorporating risk identification, assessment and mitigation for the products

6.3 In addition, the insurer shall be required to conduct the following:

i. cost/benefit analysis

ii. pilot testing on the products and provide details of the testing methodology used

iii. post implementation reviews for the products

7.0 PRICING

7.1 Pricing involves estimation of claim costs, business expenses and investment income arising from the investment of premium income from the products. Risks may occur where the costs and income are inaccurately estimated.

7.2 The insurer shall consider the following during pricing of products:

i. Set and use pricing policies and procedures for pricing;

ii. Allow for profit loading of the product during pricing;

iii. Testing the product price and profitability margins and monitor the effect of business volumes and price movements;

iv. Responsiveness of product to competitive and other external environmental pressures;

v. Develop methods for monitoring compliance with pricing policies and procedures.

8.0 UNDERWRITING

8.1 Underwriting is the process by which an insurer determines whether or not to accept a risk, terms and conditions to be applied and level of premium to be charged.

8.2 The insurer shall consider the following for each of its products:

i. develop guidelines for the underwriting procedure and basis for accepting business, rejecting or loading premiums;

ii. set a criteria for the use of further risk assessment, exclusions and reinsurance;

iii. have in place methods for monitoring emerging experience, and amending the underwriting techniques when necessary;

iv. Ensure that the underwriting approaches are consistent in the in head office including all branches.

9.0 CLAIMS MANAGEMENT

9.1 Insurers are liable to fulfill their contractual obligations to policyholders and pay claims when they fall due.

9.2 Weaknesses in the claim management process can lead to additional risk and losses to the insurer.

9.3 The insurer shall be required to:

i. set processes and procedures for claims handling, dispute resolution and maintain criteria for accepting and rejecting claims;

ii. set controls to determine fraudulent claims and take action against such claims;

iii. ensure that it is in a position to settle claims at all times, and claims due will be settled within reasonable times;

iv. have in place methods for monitoring compliance with claim management process and procedures.

9.4 In addition, the insurers shall apply the guideline issued by the Authority in regard to Claims Management.

10.0 RESERVING

10.1 The appropriate valuation of insurance liabilities is one of the most important issues facing an insurer and it's Board.

10.2 Reserving is important for the financial soundness of the insurer, and ultimately for the protection of policyholders,

10.3 The insurer shall be required to value insurance liabilities in a realistic and consistent manner.

10.4 The insurer shall be required to consider the following while reserving;

i. the nature of risk and risk distribution of claims data;

ii. particular characteristics of the class of business;

iii. reliability and volume of available claims data;

iv. past experience of the insurer and the industry;

v. robustness of the valuations models; and

vi. Materiality of the risk.

10.5 In addition, the insurers shall apply the guideline issued by the Authority in regard to Valuation of Technical Liabilities.

11.0 REINSURANCE

11.1 The insurer shall set standards for the use of reinsurance and other forms of risk transfer.

11.2 The insurer shall consider the following when developing its reinsurance arrangements:

i. The relative financial strength and claims payment record of the reinsurers in question (both in normal and stressed conditions);

ii. The soundness of the risk and capital management strategy;

iii. The appropriateness of the reinsurance strategy given the underlying insurance portfolios;

iv. The structure of the reinsurance programme;

v. The extent to which relevant functions are outsourced, either externally or within the same group of companies;

vi. The levels of aggregate exposure to a single reinsurer or different reinsurers being part of the same group;

vii. The proportion of business ceded so that the net risks retained are commensurate with the cedant's financial resources;

viii. The level of effective risk transfer;

ix. The resilience of the reinsurance programme in stressed claims situations; and

x. The extent of any credit risk mitigation in place.

11.3 In addition, the insurers shall apply the guideline issued by the Authority in regard to Reinsurance.

12.0 ENFORCEMENT

12.1 When the Authority ascertains non-compliance from the insurer, it may take necessary action in accordance with the provision from the Insurance Act.

13.0 EFFECTIVE DATE

13.1 The effective date of this guideline is 30th June 2013.

14.0 ENQUIRY

Enquiries on any aspect of this guideline shall be referred to;

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