



IRA

Insurance Regulatory Authority

IRA/PG/16

**GUIDELINE ON VALUATION OF TECHNICAL
LIABILITIES FOR GENERAL INSURERS**

MAY 2013

To: All Insurance & Reinsurance Companies

GUIDELINE ON VALUATION OF INSURANCE TECHNICAL LIABILITIES FOR GENERAL BUSINESS

This guideline on valuation of insurance technical liabilities is issued pursuant to section 3A of the Insurance Act for observance by Insurance and Reinsurance Companies transacting general business.

The guideline sets principles for the consistent measurement and reporting of the insurance liabilities of all general insurers.

It is worth noting that financial soundness of the insurer and ultimate protection of policyholders is dependent on proper, realistic and consistent valuation of the insurance technical liabilities.

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

A handwritten signature in black ink, appearing to read 'Sammy M. Makove', is positioned above the name and title.

SAMMY M. MAKOVE
COMMISSIONER OF INSURANCE & CHIEF EXECUTIVE OFFICER

THE INSURANCE ACT (CAP 487)
IRA/PG/16
GUIDELINE TO THE INSURANCE INDUSTRY

Valuation of Technical Liabilities for General Insurers

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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 respect of liability valuation for General Insurers.

2.0 INTRODUCTION

- 2.1 This Guideline establishes a set of principles for the consistent measurement and reporting of the insurance liabilities of all general insurers.
- 2.2 The appropriate valuation of insurance liabilities is one of the most important issues facing an insurer. It is important for the financial soundness of the insurer, and ultimately for the protection of policyholders, that insurance liabilities are valued in a realistic and consistent manner.
- 2.3 It is ultimately the responsibility of the insurer's Board and Senior Management to place an appropriate valuation on the insurer's liabilities, after considering actuarial and other advice.

3.0 KEY REQUIREMENTS

The key requirements of this guideline are:

- 3.1 The Board of an insurer shall obtain a statement from the Appointed Actuary on the valuation of the insurer's insurance liabilities.

3.2 Insurance liabilities include both the insurer's Outstanding Claims Liabilities, and its Premiums Liabilities.

Outstanding Claims Liabilities means claims incurred prior to the calculation date, which have been reported and not yet settled or which have been incurred but not yet reported.

Premiums Liabilities means the cost of running off the unexpired portion of an insurer's policies and is composed of Unearned Premium Reserve and Unexpired Risk Reserve among others.

3.3 It is the ultimate responsibility of the **Board of the insurer** to determine the appropriate valuation of insurance liabilities.

3.4 In the event the Board decides to reject the Appointed Actuary's statement, or to otherwise adopt a valuation of insurance liabilities that is not in accordance with the principles of this Guideline, the insurer shall in writing **disclose** the following to the Authority prior to finalizing of the financial statements:

- i. The reasons for not accepting the Appointed Actuary's statement, or for not determining the insurance liabilities in a manner consistent with this Guideline; and
- ii. Details of the alternative assumptions and methodologies used in determining the value of the insurance liabilities.

4.0 VALUATION OF INSURANCE LIABILITIES

4.1 Premium Reserves

- 4.1.1 In determining the value of unearned premium reserves the following methods shall be applied
- i. “24ths” method (reserving on a monthly basis);
 - ii. “365ths” method (reserving on a daily basis);
- 4.1.2 The insurer shall determine and disclose a value for its Unearned Premiums Reserves for each class of business.
- 4.1.3 When determining unearned premium reserves, an insurance company shall conduct a test on the adequacy of the reserves. Where the unearned premium reserves are inadequate, premium deficiency reserves shall be determined.
- 4.1.4 The reserving method used to determine the unearned premium reserves shall be required to be consistent i.e. shall not be changed arbitrarily.
- 4.1.5 The reinsurers may apply the “8th” method when reserving on a quarterly basis.
- 4.1.6 The reserve for unexpired risks shall be calculated by estimating the Claims Expected to be incurred after the Valuation Date on policies with Unexpired Exposure Periods as at the valuation date, including the part of claims management expenses that relates to these claims in such an amount that the estimated value of such future claims exceeds the unearned premiums reserve.

4.1.7 The reserve for unexpired risks shall be calculated and maintained separately on each class of insurance

4.2 Claim Reserves

4.2.1 Reserves in respect of outstanding claims incurred and reported shall be determined prudently by using Case Estimate Method, Average Cost per Claim Method or other methods recognized by the Authority.

4.2.2 Reserves in respect of incurred but not reported claims shall be valued and determined prudently by using at least two of the following methods in accordance with the risk nature, risk distribution and experiential data of the insurance lines:

- i. Chain-Ladder Method;
- ii. Average Cost Per Claim Method;
- iii. Bornhuetter-Ferguson Method
- iv. Standard Development Method;

4.2.3 An insurer that has been in existence for not more than three years can use the Standard Development Method.

4.2.4 The percentage of net premiums written during the year should be applied when using Standard Development Method as provided in the appendix to this guideline.

4.2.5 The methods to be adopted for the valuation of the Claim reserves shall depend on:

- i. The particular characteristics of the class of business
- ii. The reliability and volume of the available data;
- iii. Past experience of the insurer and the industry; and
- iv. The robustness of the valuations models; and
- v. Considerations of materiality.

4.2.6 The value of the Claim Reserves shall include an amount in respect of the anticipated Claim adjustment expenses.

4.2.7 When determining claims reserves, an insurance company shall conduct a test on the adequacy of the reserves. Where the claims reserves are inadequate, claims deficiency reserves margin shall be determined.

4.2.8 The insurer shall determine and disclose a value for its Claims Reserves for each class of business.

5.0 REPORTING ON RESERVES

- 5.1. The appointed actuary shall be in charge of reserving.
- 5.2. An insurer shall annually submit to the Authority reserves valuation report signed by the appointed actuary of the company. The report shall contain the following:
 - i. A statement that the applied method is in compliance with the stipulations of this guideline.
 - ii. An actuarial opinion on the reserving;
 - iii. A detailed description of the reserves valuation;
 - iv. Definite explanation of special terms and concepts in the report.
- 5.3. Description of the annual reserves valuation shall contain the following:
 - i. Definite criteria for division of insurance lines or categories and names of the insurance lines or categories;
 - ii. Completeness and accuracy of the data of different insurance lines or categories, and a description of the problems these data may have;
 - iii. The actuarial method and model for valuation; if the actuarial method and model differ from those previously adopted, reasons for making the change and its effects on the reserves results shall be described;
 - iv. Major assumptions of the actuarial method and model, and reasons for adopting such assumptions;
 - v. The discrepancy between the actuarial result of the previous reserving and the actual experience;
 - vi. Adequacy of reserving;

- vii. For unearned premium reserves, changes concerning periodicity, basic premium rate, risk adjustment coefficient, loss ratio, expense ratio, surrender ratio and other factors of insurance lines shall be described.
 - viii. For outstanding claims reserves, changes concerning the occurrence rules of compensation cases, case closing rules, changing rules of average cost per claim, underwriting practices, claim settlement practices, ceding arrangement, additional cost increment and other factors shall be described.
- 5.4. An insurer shall submit to the Authority quarterly reserve valuation reports signed by the Head of the Actuarial function and the Principal Officer of the company. The report shall contain the following:
- i. Statement that the applied method is in compliance with the stipulations of this guideline.
 - ii. Reserve value per line of business.
 - iii. Any other information that may influence the value of the reserves.

6.0 ENFORCEMENT

6.1 Remedial Measures

6.1.1 When the Authority determines that the insurer's non-compliance with the provisions of this guideline, the Authority may take further steps in accordance with the provisions of the Insurance Act.

6.2 Administrative Sanctions

6.2.1 Where the Authority determines that an insurer has not met the requirements of this directive, the Authority may impose any or all

of the administrative sanctions to correct the situation in accordance with the provisions of the Insurance Act, including but not limited to:

- i. Prohibition from declaring and/or paying dividends;
- ii. Declaration that a person may not take the office of Appointed Actuary;
- iii. Suspension of the establishment of new branches and/or expansion into new financial activities;
- iv. Suspension or closure of the insurer to new business
- v. Suspension or closure of an insurer;
- vi. Suspension of acquisition of fixed assets; and
- vii. Monetary penalties.

7.0 EFFECTIVE DATE

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

8.0 ENQUIRY

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

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APPENDIX (Clause 4.2.4)

No	Class of insurance business	Percentage of Net Premium Written
1	Aviation	2%
2	Engineering	5%
3	Fire Domestic	1%
4	Fire Industrial	1%
5	Liability	5% - Current Year 3% - One year preceding the current year 1% - Two years preceding the current year
6	Marine	2.5%
7	Motor Private	5%
8	Motor Commercial	5% - Current Year 3% - One year preceding the current year 1% - Two years preceding the current year
9	Motor Commercial (PSV)	20% - Current Year 12.5% - One year preceding the current year 5% - Two years preceding the current year
10	Personal Accident Insurance	5%
11	Theft	5%
12	Workmen's Compensation	5% - Current Year 3% - One year preceding the current year 1% - Two years preceding the current year
13	Medical	3%
14	Micro insurance	4%
15	Miscellaneous	5%