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FINANCIAL SERVICES COMMISSION

BULLETIN ON:

Relaxation of the Minimum Capital Test Requirement

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RELAXATION OF THE MINIMUM CAPITAL TEST REQUIREMENT

1.0 BACKGROUND

1.01 The Financial Services Commission (FSC) is mandated by section 6 of the FSC Act to protect the customers of the financial services by, inter alia, promoting the stability and public confidence in the operations of the institutions it regulates. One important way of achieving this is by means of establishing a risk-based measure which is used to assess the capital strength of the general insurance industry to determine whether their contractual obligations will be honoured when they are faced with adverse events.

1.02 In 2011 the FSC changed the solvency requirements for general insurance companies from the required Minimum Asset Test ("MAT") to the Minimum Capital Test ("MCT"). The MCT is a risk-based measure that considers the risks faced by an insurance company based on the lines of business it undertakes, as well as the types and amounts of assets and liabilities that it holds. The MCT computes the total capital required by a company to adequately cover its risks, and then compares this to the capital actually available to the company. The capital required is calculated as the product of the company's assets and liabilities and their assigned risk weightings. Capital required also incorporates margins to reflect the risks being covered by the insurance portfolio. Companies with risky assets or volatile lines of business will be required to hold more capital than companies with more conservative business models.

1.03 Prior to the implementation of the MCT and the promulgation of its accompanying legislation in 2011, the FSC over a period of three years held consultative fora with our major stakeholders being representatives of the insurance industry. Subsequent to full implementation of the regulatory capital requirement (MCT), the FSC continues to maintain a relationship with the insurance industry that fosters engagements regarding amendments to the legislation in line with international standards and ultimately to encourage innovation and growth within the insurance industry. As such, the FSC may periodically review the capital standards for insurance entities in consultation with the industry; this may at times require the relaxation of certain policies, procedures or legislation while not endangering the obligations due to policyholders. Nonetheless, in accordance with this core mission, the FSC must honour its commitment to ensure that the strength and integrity of the industry is maintained. Hence, careful consideration is given to any amendments to the regulatory framework in order to ensure that such changes will not jeopardize the industry and the people it serves.

2.0 REGULATORY FORBEARANCE

2.01 It is against this background that the FSC has sought to exercise regulatory forbearance by allowing a relaxation of the statutory minimum of 250% for the MCT, thus reducing the amount of capital that the general insurance industry would need to hold for the purpose of meeting capital adequacy requirements.

2.02 During this period of regulatory forbearance, the FSC will carry out a Quantitative Impact Study (QIS) to determine an optimal position for the MCT that balances growth and stability of the insurance industry. It should be noted however, that the relaxation of the regulatory capital requirement is conditional on the following:

i. The FSC will exercise regulatory forbearance for a period of no more than 2 years, within which time the general insurance companies will be allowed to maintain a MCT ratio of at least 150%. This relaxation of the MCT requirement should not be construed as a removal of the current prescribed capital requirement, and will not supersede any outcome that emanates from the QIS project.

ii. The main reason for the reduction of an insurer's MCT ratio should be due to the reorganization of the company's investment portfolio to pursue local growth initiatives. The companies will be required to provide details of the initiatives used to pursue growth and the impact these activities will have on the MCT ratio on a monthly basis.

iii. During the period of forbearance, the amount of dividends paid to shareholders of the general insurance company should not exceed 50% of profit that was achieved for the previous financial year. The companies are also expected to meet all the other requirements of the Insurance Act and accompanying regulations.

iv. The general insurance industry should recognize that the continuation of this exercise will be contingent on its strict adherence to maintaining a MCT of at least 150%. Further, the FSC reserves the right to impose additional requirements or discontinue access to this interim capital requirement on a case by case basis, in the event of any material circumstance that may pose a threat to the viability of an insurer.

v. Insurers should note that the FSC will continue to require monthly filings of all relevant information in relation to the MCT.