



QUANTIFYING RISK, ENABLING OPPORTUNITY

Subject: Insurance Group Supervision

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Legislative Framework

General

The current requirements in the Banks Act, Insurance Bill and FSR Bill will introduce 3 levels within the supervisory hierarchy, namely:

- Level 1:** Supervision of a licensed entity on a standalone basis(referred to as solo supervision)
- Level 2:** Specialist group supervision where the supervised group operates primarily in one industry e.g. banking or insurance groups
- Level 3:** Supervision of a financial conglomerate, where the group of companies includes of a combination of an insurer, a bank or a financial market infrastructure

Insurance Bill

Insurance group:

“means the group of entities designated by the Prudential Authority under section 10”

Section 10:

Designated insurance group:

- Insurer
- Any company that is part of the group of companies the insurer is in; and
- Any subsidiary and associate...”

Legislative requirements

Requirement	To whom it applies
General information request	Insurance Group
Licensing	Controlling Company
Significant owners	Controlling Company
Group structure	Insurance Group
Governance requirements	Controlling Company
Solvency requirements	Insurance Group
Material acquisitions/disposals	Insurance Group
Capital add-on	Controlling Company
Reporting requirements	Insurance Group
Supervisory Cooperation	Insurance Group
Intragroup transactions and concentrations	Insurance Group
Resolution of controlling company	Controlling Company

Insurance Group's Solvency Requirements

General

- Capital requirements are calculated using the deduction and aggregation method (D&A method) – this is the default
- Insurance Groups can apply to use the Accounting and Consolidated Method (only SA Insurers)
- Proposed solvency requirements are set out in Financial Soundness Standards for Groups (FGSs)

Scope of insurance group

- IFRS consolidated accounts starting point
- Apply the materiality limits to exclude
- Consider scoping in entities with significant influence over the group (operational and financial)
- Treatment of sub-groups (as scoped by the PA)

Roles and responsibilities

- Responsibility for the financial soundness rests with the board of directors of the controlling company

Board of directors must:

- Ensure appropriate level and quality of Own Funds commensurate with risks
- Ensure fungibility and transferability of Own Funds across the insurance group to absorb group losses

Roles and responsibilities

Board of directors must:

- Implement procedures to monitor financial soundness
- Identify any deterioration in its actual or expected capital resources or business conditions
- Notify, within 3 months, circumstances that could lead to breaches of the financial soundness requirements
- Seek approval before effecting any capital reduction at controlling company level (other than normal dividend payment)

Roles and responsibilities

Head of Actuarial Control responsibilities:

- Providing assurance on the accuracy of calculations
- Provide assurance on the appropriateness of the assumptions used to determine Eligible Own Funds and SCR at the insurance group level

Auditor's responsibilities:

- Audit the financial soundness of the insurance group
- Report on any matters identified that may cause the insurance group to be not financially sound

D&A Method

Key principles are:

- Aggregation of each of the entities in the scope
- Elimination of intragroup transaction
- Type of entity will determine the valuation and capital requirements
- Only eligible own funds can count - transferability and fungibility considerations required
- No diversification benefit

D&A Method

Measures for solo Own Funds and solo SCR

Type of entity	Own funds	SCR	Comment
SA insurer	SAM	SAM	
Non- SA insurer (equivalent)	Country rules	Country rules	PA publish a list
Non- SA insurer (non-equivalent)	SAM or PA approved method	SAM or PA approved method	WIP
Other regulated entities	Sectorial rules	Sectorial rules	Under consideration
Other non-regulated entities	IFRS NAV	Equity shock under SAM solo requirements	Not aligned to banking requirements. Does not capture risks
Controlling company	IFRS NAV	Equity shock or see through basis	

Group eligible Own Funds

Step 1 – Eliminate intra-group transactions

Following to be eliminated:

- Loans
- Guarantees and off-balance sheet transactions
- Capital investments
- Reinsurance
- Cost-sharing arrangements
- Risk-transfer transactions
- Other transactions

Group eligible Own Funds

Step 2 – Assess restrictions on the availability of certain group Own Funds

- Own Funds that are non-fungible or non-transferable
- Assessment:
 - Restrictions due to legal or regulatory requirements i.e. ring-fenced funds, exchange controls or unable to be available within 9 months
 - Ancillary Own Funds of participations i.e. hybrid capital instruments and subordinated liabilities not issued or guaranteed and deferred tax assets

Group eligible Own Funds

Step 3 – Aggregate adjusted solo Own Funds

- **Aggregation is the sum of:**
 - Adjusted Own Funds of the controlling company;
 - Adjusted solo Own Funds of each participation (pro-rata)

Group eligible Own Funds

Step 4 – Apply eligibility limits

Type of entity	Eligibility limits related to tiering
SA insurer Non- SA insurer (non-equivalent) Controlling company (not insurer) Intermediate holding company Non regulated entity	SCR and MCR: <ul style="list-style-type: none">• T3 BOF to cover SCR, not to cover MCR• Ancillary OF to cover SCR, not to cover MCR Composition of Eligible OF : <ul style="list-style-type: none">• = 50% of SCR to be T1 Eligible OF• < 15% of SCR to be T3 Eligible OF• T2 + T3 Eligible OF < 50% of SCR 80% of the MCR = T1 Eligible OF Other paid-in capital T 1 instruments < T1 Eligible OF. Other portion to be recognised as T2 Eligible OF

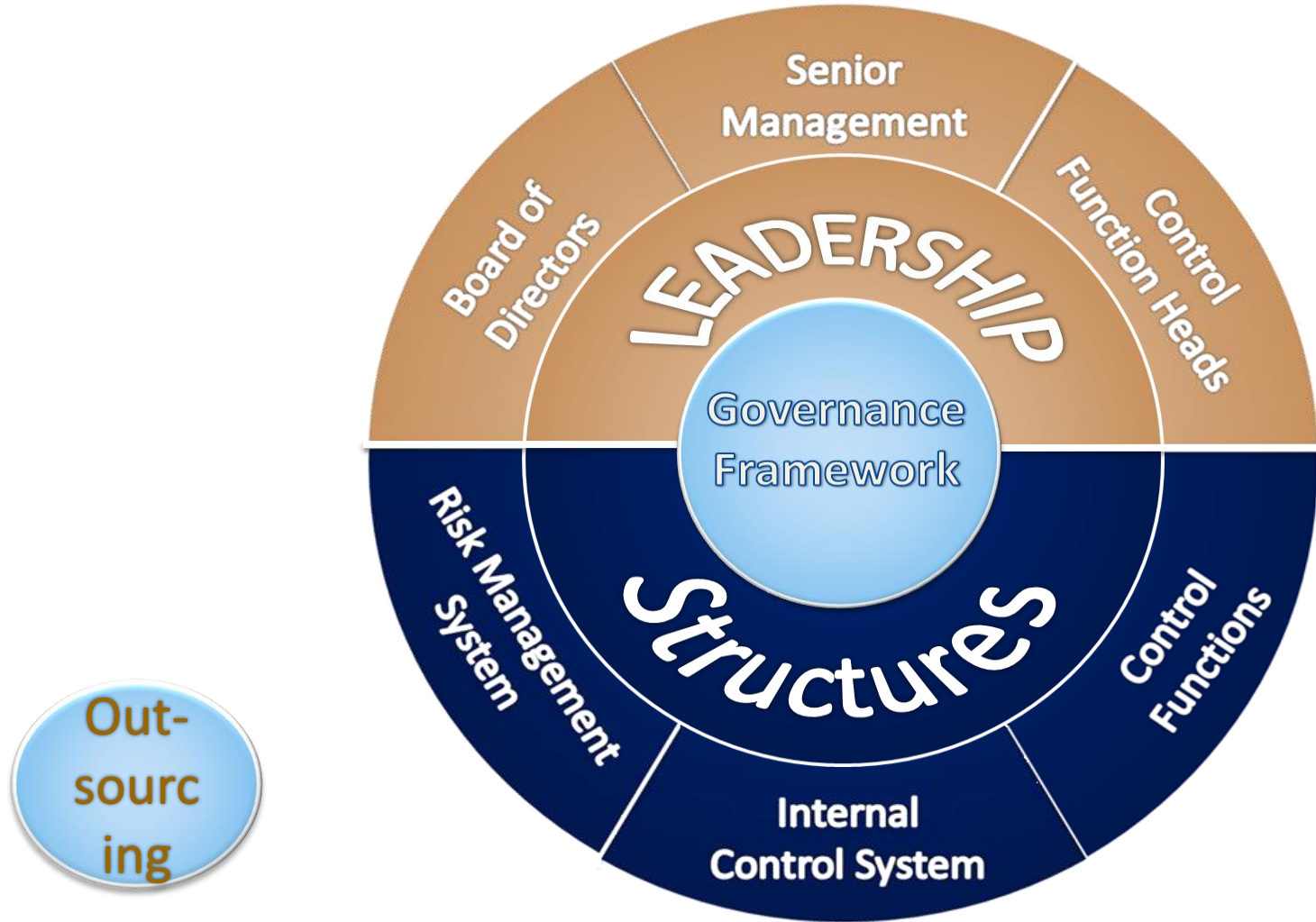
Group eligible Own Funds

Step 4 – Apply eligibility limits

Type of entity	Eligibility limits related to tiering
Non- SA insurer (equivalent)	Country rules
Regulated financial or credit institution	Sectorial rules

Insurance Group's Governance Requirements

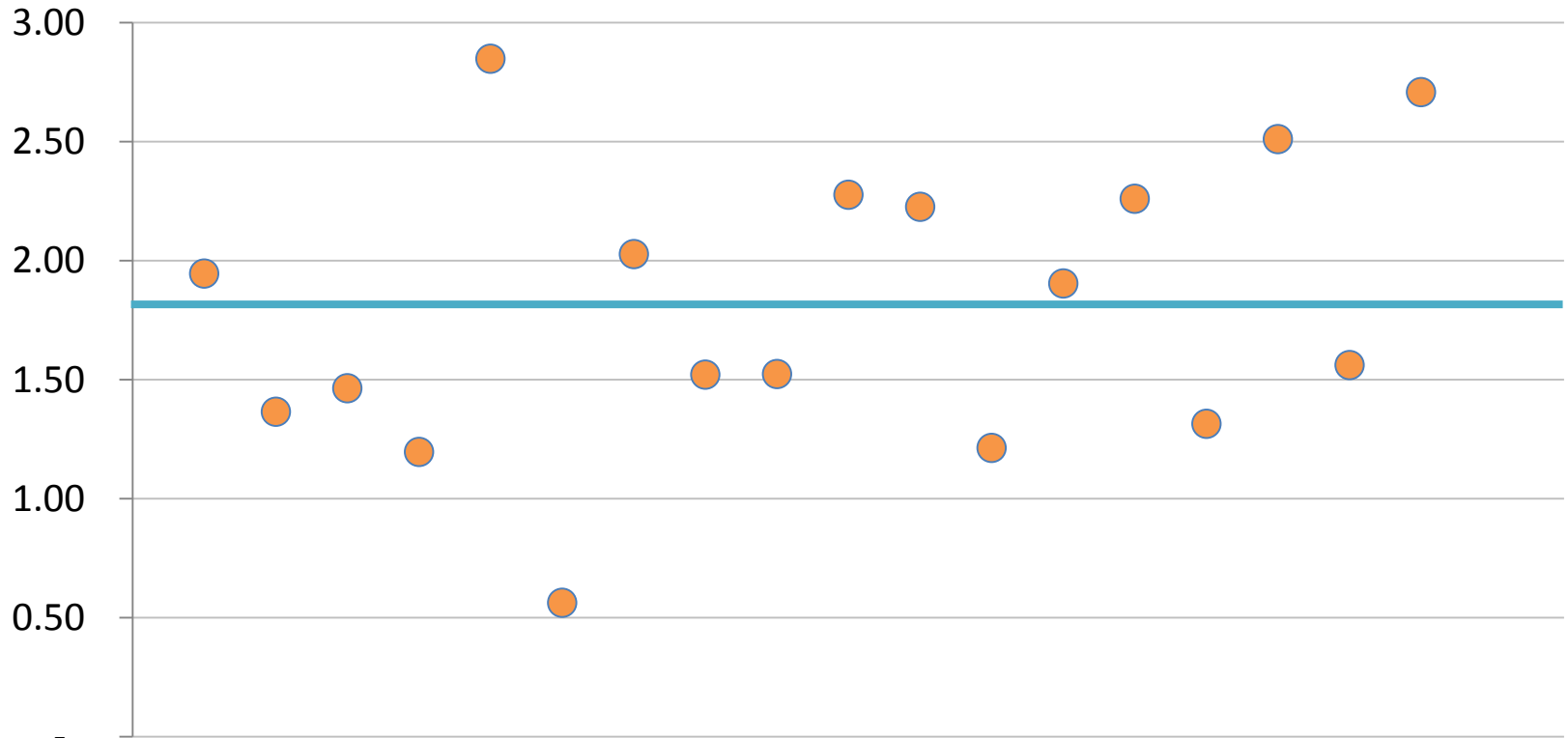
Governance Framework



What are we seeing....

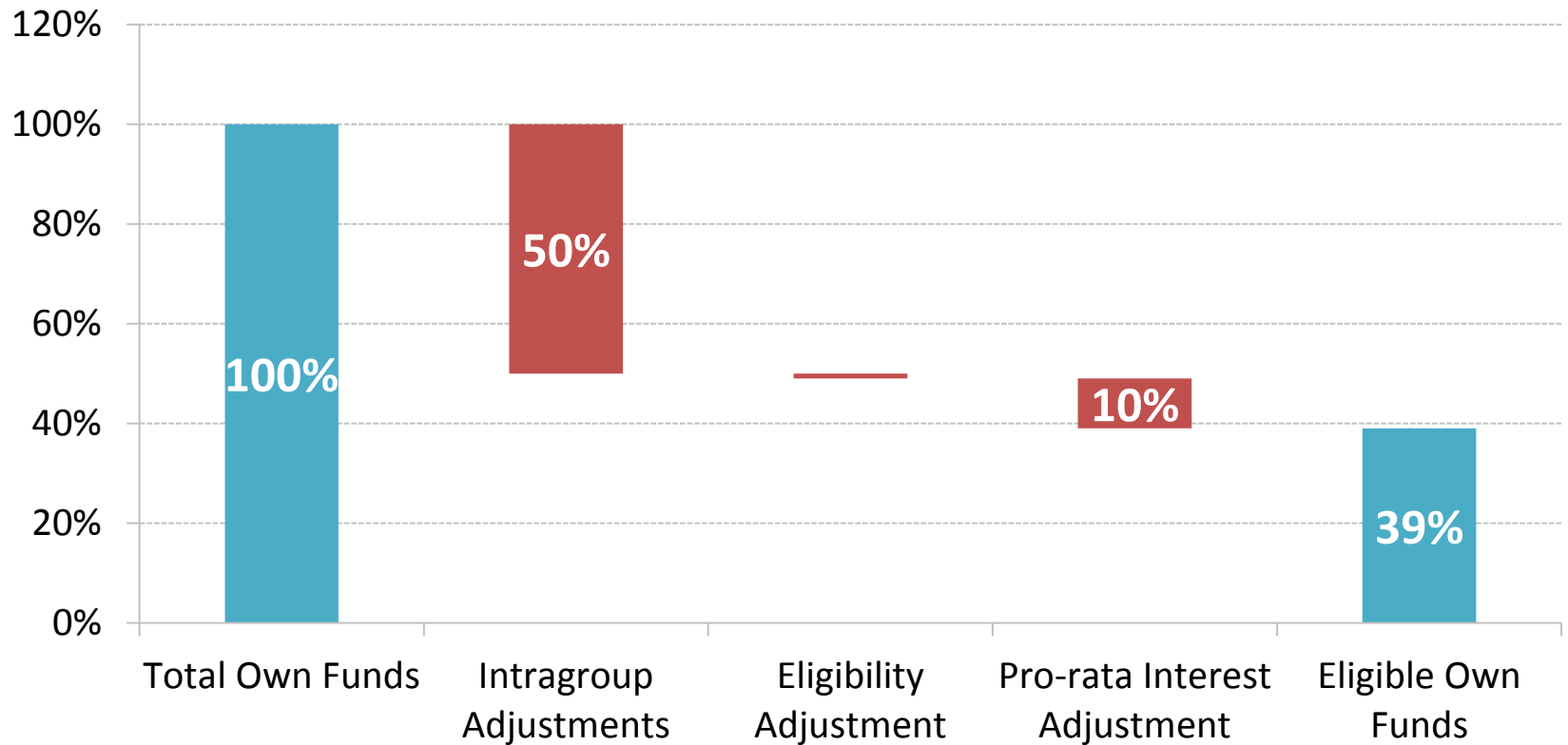
Group Supervision

SCR Cover



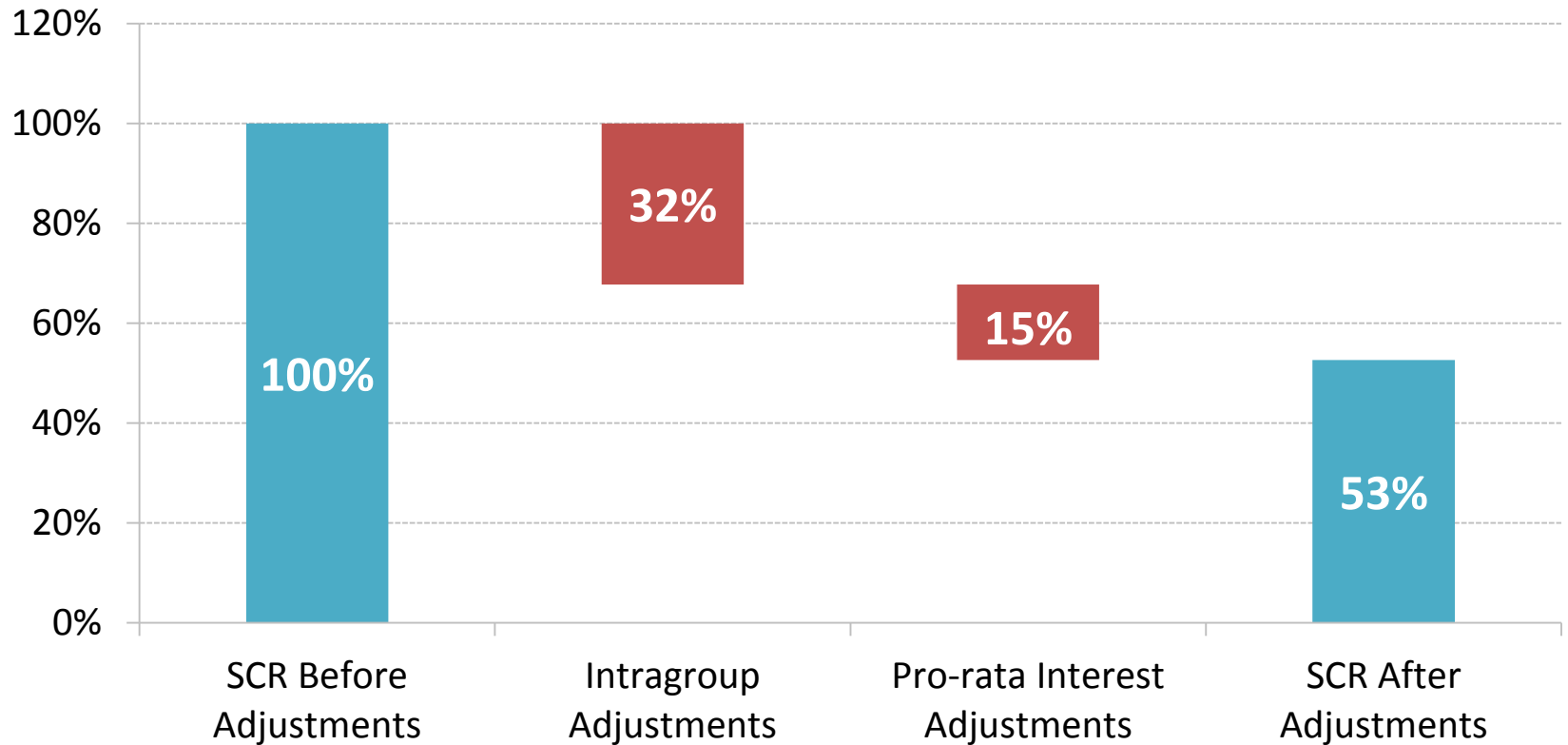
Group Supervision

Adjustments to Own Funds



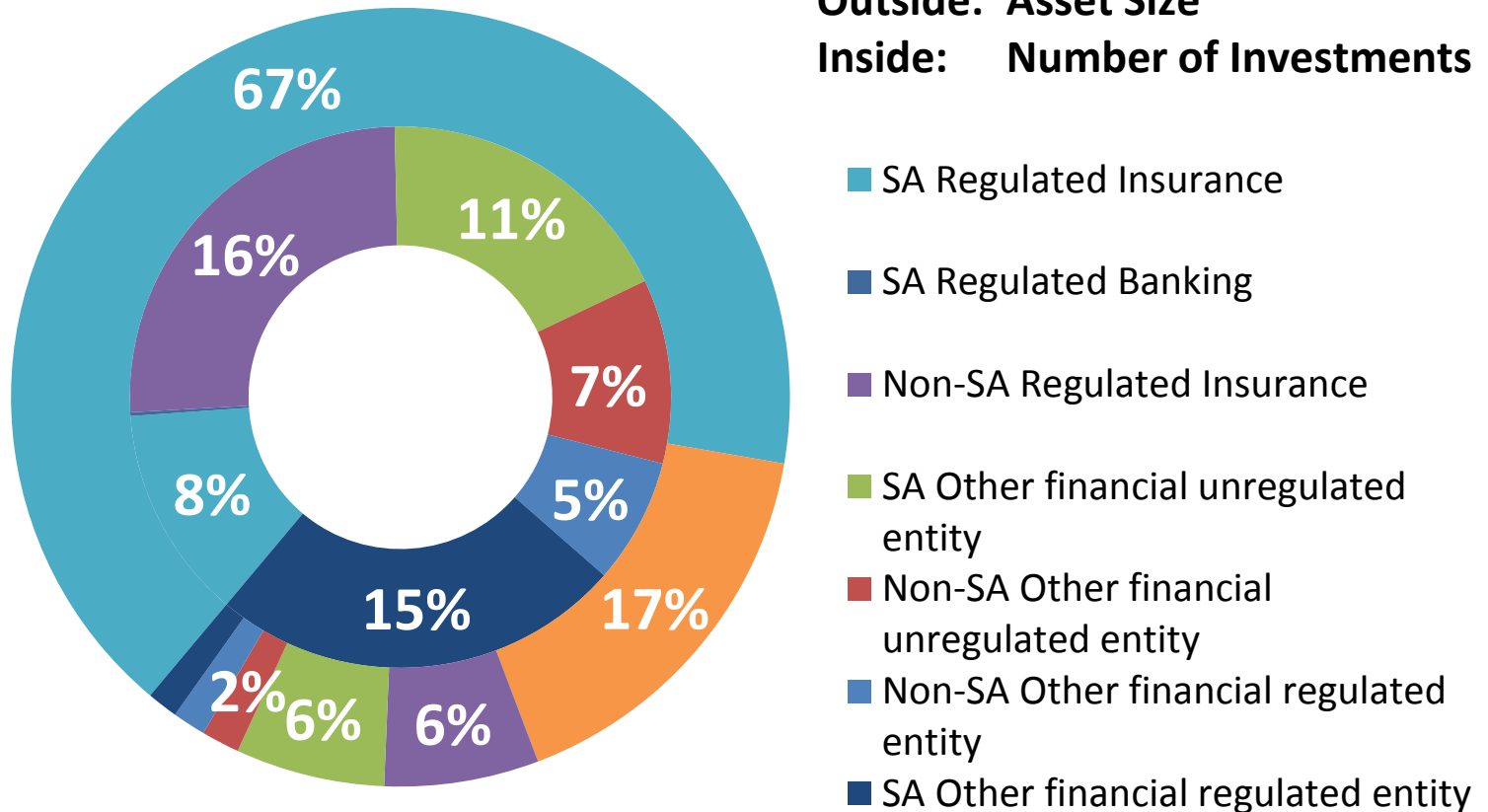
Group Supervision

Adjustments to SCR



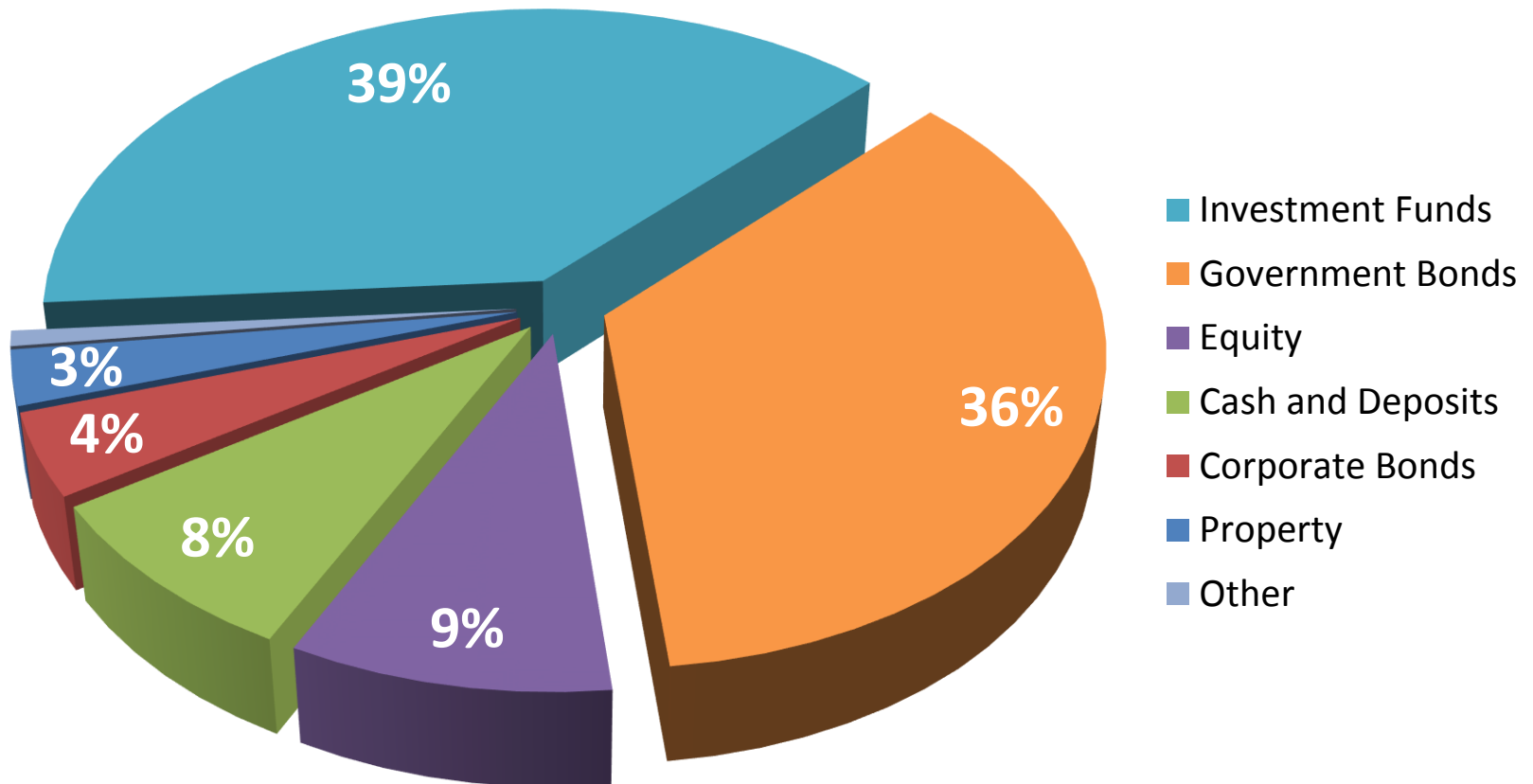
Group Supervision

Number and Asset Size of Investments per Investment Type



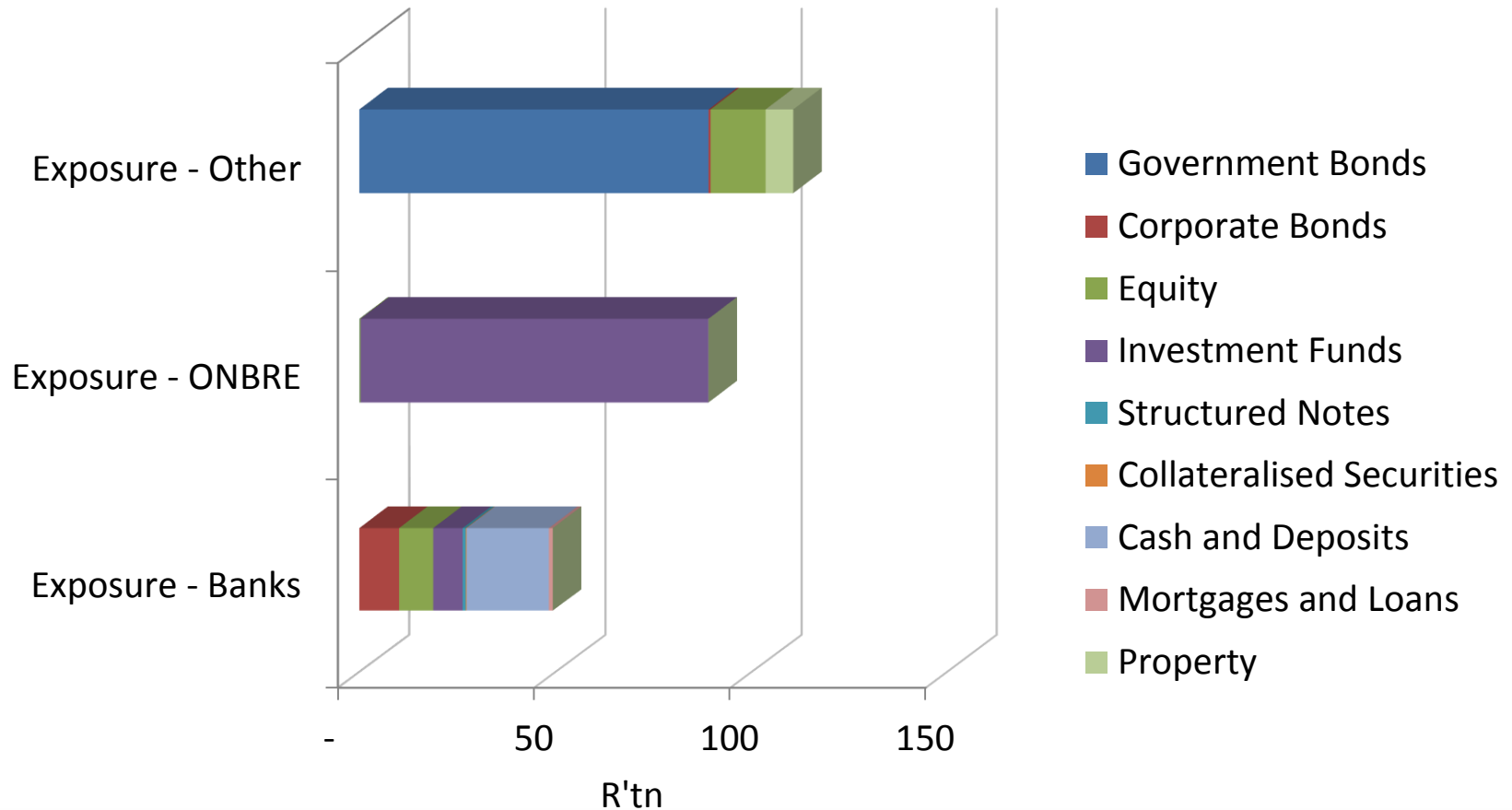
Group Supervision

Exposure of Large Groups



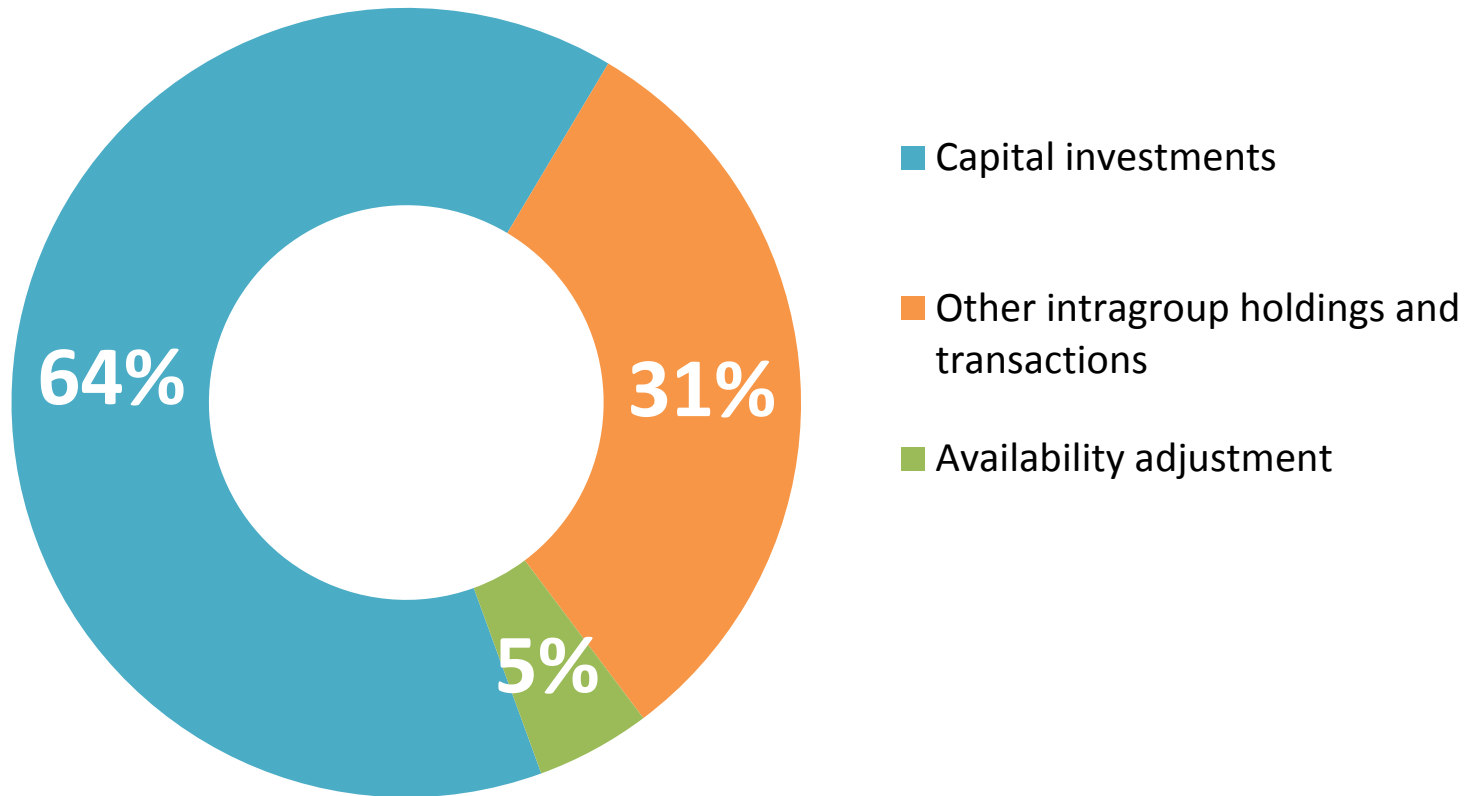
Group Supervision

Exposure of Large Groups



Group Supervision

Types of Intragroup Adjustments



Financial Conglomerate Supervision

General

The current requirements in the FSR Bill:

Level 3: Supervision of a financial conglomerate, where the group of companies includes of a combination of an insurer, a bank or a financial market infrastructure

FSRB defines:

“**financial conglomerate**” means a group of companies designated as a financial conglomerate in terms of section 160;

General

Section 160 of FSRB

“A financial conglomerate designated in terms of subsection (1) must include both an eligible financial institution and a holding company of the eligible financial institution, but need not include all the members of the group of companies

FSRB defines - **“eligible financial institution”** means each of the following:

(a) A financial institution licensed or required to be licensed as a bank in terms of the Banks Act;

(b) a financial institution licensed or required to be licensed as a long-term insurer in terms of the LTIA or a short-term insurer in terms of the;

(c) a market infrastructure; and

(d) a financial institution prescribed in Regulations for the purposes of this definition.

Why needed

- Captured risks not covered by Level 1 and 2
- Minimise failure and financial stability impact
- Holistic view of group-wide activities
- Consistent application of requirements
- Capture variety of corporate structure arrangements
- Interconnectedness of financial sector
- Integrated model of prudential supervision

Prudential standards

- Capital adequacy including capital and liquidity planning
- Leverage
- Risk management processes, practices and systems
- Governance
- Public Disclosure

Way forward

Legislation

- Financial Sector Regulation Bill (FSR Bill) expected to be enacted during Q2 or Q3, 2017
- Insurance Bill can only be considered after FSR Bill is passed
- The estimated implementation date of SAM has been revised to 1 July 2018 to accommodate the legislative timeline for the Insurance Bill

Prudential Standards- Round 2.5

UPDATED FINANCIAL SOUNDNESS STANDARDS AND GOVERNANCE & OPERATIONAL STANDARDS TO BE RELEASED FOR INFORMAL PUBLIC CONSULTATION 28 JUNE – 9 AUGUST 2017

- Financial Soundness Standards for Insurers (FSI)
- Financial Soundness Standards for Insurance Groups (FSG)
- Financial Soundness Standards for Lloyd's (FSL)
- Financial Soundness Standards for Microinsurers (FSM)
- Financial Soundness Standards for Branches of Foreign Reinsurers (FSB)
- Governance and Operational Standards for Insurers (GOI)
- Governance and Operational Standards for Insurance Groups (GOG)
- Governance and Operational Standards for Lloyd's (GOL)
- Governance and Operational Standards for Microinsurers (GOM)
- Governance and Operational Standards for Branches of Foreign Reinsurers (GOB)

Prudential Standards - Round 3

FOR FORMAL PUBLIC COMMENT (as provided for in the FSR Bill)

- Full suite of Prudential Standards
- Q1 2018 (provisionally)

Financial Conglomerate Supervision

- Discussion Document was issued to the industry associations
- Comments due by 15 June 2017
- Consultative process
- Same approach as SAM with various work streams
- Outcome to be translated into Prudential Standards

Thank you