

**CAYMAN ISLANDS MONETARY AUTHORITY**  
**PRIVATE SECTOR CONSULTATION**



**RULE ON RISK MANAGEMENT FOR INSURERS**

**A. INTRODUCTION**

1. Section 34(1)(a) of the Monetary Authority Law (2013 Revision) (as amended) ("MAL") states that –

After private sector consultation and consultation with the Financial Secretary, the Authority may –

- (a) *issue or amend rules or statements of principle or guidance concerning the conduct of licensees and their officers and employees, and any other persons to whom and to the extent that the regulatory laws may apply;*

2. Requirements specific to the private sector consultation are outlined in section 4(1) of the MAL as follows:

*When this Law requires private sector consultation in relation to a proposed measure –*

- (a) *the Authority shall give to each private sector association a draft of the proposed measure, together with –*

- i. an explanation of the purpose of the proposed measure;*
- ii. an explanation of the Authority's reasons for believing that the proposed measure is compatible with the Authority's functions and duties under section 6;*
- iii. an explanation of the extent to which a corresponding measure has been adopted in a country or territory outside the Islands;*
- iv. an estimate of any significant costs of the proposed measure, together with an analysis of the benefits that will arise if the proposed measure is adopted; and*
- v. notice that representations about the proposed measure may be made to the Authority within a period specified in the notice (not being less than thirty days or such shorter period as may be permitted by subsection (3));and*

- (b) *before proceeding with the proposed measure, the Authority shall have regard to any representations made by the private sector associations, and shall give a written response, which shall be copied to all the private sector associations.*

3. The Authority hereby seeks consultation and comment from the private sector associations concerning the proposed amendments to the Rule on Risk Management for insurers.
4. The proposed amended Rule is attached.

## **B. BACKGROUND**

5. Risk management has become a critical component of businesses in the financial services industry. It has been said that inadequate systems or the poor management of risks contributed to the failures of a number of large institutions that led to the recent financial crisis.
6. The proposed Rule amends the Rule on Risk Management issued in 2009. The Rule sets out key principles that insurers must adopt in the implementation of a risk management framework with a focus on the need to identify, measure, assess, report and control the risks that they are exposed to in their business.

## **C. INTERNATIONAL INITIATIVES**

7. The proposed Rule is consistent with IAIS Insurance Core Principle 8 (ICP) which states:

*"The supervisor requires an insurer to have, as part of its overall corporate governance framework, effective systems of risk management and internal controls, including effective functions for risk management, compliance, actuarial matters and internal audit."*

8. The proposed Rule will also increase the Cayman Islands' compliance with ICP 7 - Corporate Governance, ICP 16 - Enterprise Risk Management for Solvency Purposes, ICP 21 - Countering Fraud in Insurance and ICP 23 - Group Wide Supervision.

## **D. PURPOSE OF PROPOSED MEASURE AND CONSISTENCY WITH THE AUTHORITY'S FUNCTIONS**

9. The purpose of the amendments to the Rule is to ensure that an insurer has in place a comprehensive and robust risk management framework that is communicated within the organization and regularly reviewed.
10. The proposed Rule introduces amendments and clarifications with respect to:
  - a) The link between risk management and strategic business objectives
  - b) The documentation required as part of the risk assessment framework
  - c) The concept of a feedback loop to allow the Board of Directors to review the risk management framework based on the insurer's experience
  - d) A requirement for insurers to consider fraud risk and money laundering risk
  - e) The application of the Rule to insurers that are part of a group
  - f) A requirement for the insurer to communicate its risk management policies to relevant staff and to train key staff on the risk management framework
  - g) The connection between risk management and capital.
11. Section 6(1) of the MAL provides that the principal responsibilities of the Authority include its regulatory functions, inter alia, "to regulate and supervise financial services business carried on in or from within the Islands."

12. Section 6(3) of the MAL provides that in performing its regulatory functions, the Authority shall, inter alia:

- a) endeavour to promote and enhance market confidence and the reputation of the Islands as a financial centre;
- b) recognise the international character of financial services and markets and the necessity of maintaining the competitive position of the Islands, vis-à-vis both consumers and suppliers of financial services, while conforming to internationally applied standards insofar as they are relevant and appropriate to the circumstances of the Islands;
- c) recognise the principle that a burden or restriction which is imposed on a person or activity should be proportionate to the benefits, considered in general terms; and
- d) recognise the desirability of facilitating innovation in financial services business.

### E. IMPLEMENTATION IN OTHER JURISDICTIONS

13. Details on the regulatory requirements relating to risk management of several countries were examined. The jurisdictions below were selected on the basis that either:

- a. It was assessed by the IMF in accordance with the revised 2011 IAIS ICPs (Hong Kong, Bahamas, Canada, Singapore, Barbados); or
- b. It has a similar domestic insurance market operating alongside a significant captive market: (Bermuda, Guernsey).

#### IMF Country Assessment Comparison

COUNTRY	COMMENTS	RECOMMENDATIONS
Hong Kong	<p>The Insurance Companies Ordinance must be updated to better to better reflect current international best practices <i>[including]</i> updating risk management requirements.</p> <p>Guidance Notes does not have explicit provision on the establishment of an effective risk management function covering all material risks</p> <p>There are currently no explicit requirements on insurers to:</p> <ol style="list-style-type: none"> <li>1. adopt a risk management policy that details how all relevant and material risks are managed on a regulatory and economic basis; and</li> <li>2. establish and maintain a risk tolerance statement and risk tolerance limits which take into account all relevant and material categories of risk.</li> </ol>	<p>The authorities are advised to:</p> <ol style="list-style-type: none"> <li>a) Widen the scope of the risk management requirements to cover all key risks (i.e. underwriting, market, credit, operational and liquidity risks, at the minimum);</li> <li>b) Establish minimum requirements on risk management systems and key control functions as enforceable rules;</li> <li>c) Require insurers to have compliance and actuarial functions.</li> </ol> <p>These requirements could be supplemented by supervisory guidance to facilitate compliance by insurers.</p>
Bahamas	<p>There are no regulations or formal policies requiring effective risk management. Further, there are no</p>	<p>Amend the regulations to impose an effective risk management requirement</p>

	requirements for the insurer to have effective control functions with the necessary authority, independence and resources.	and publish standards and best practices guidance for development of a risk management program and establishment of insurers' internal controls
Canada	OSFI has an extensive framework of requirements for risk management and control functions at FRIs and oversees the effectiveness of the arrangements as part of its supervision program. A particular emphasis of the approach is on ensuring that there is a Chief Risk Officer at the major institutions with appropriate stature and authority, including a reporting line to the board. OSFI's approach also provides for a balance between ensuring appropriate stature and significance for actuarial work, supported by the key role of the Appointed Actuary, and fully embedding actuarial work and decisions within the overall corporate governance framework.	None
Singapore	The Notices and Guidelines require the key functions to have authority, resources, seniority and direct access to the Board or relevant Board Committees. MAS monitor the effectiveness of the key functions through onsite inspections and offsite monitoring, which are reflected in CRAFT ratings and inspection plans.	None
Barbados	Legally binding guidelines for corporate governance, market conduct, risk management, and valuation of assets have been issued and implemented.	The guideline on Internal Control and Risk Management should be deepened and further elaborated further. The FSC should follow up the survey results through offsite monitoring and/or onsite examinations to encourage the whole industry to improve their internal control and risk management in accordance with the nature, scale and complexity of their risk profile.

### **Similar Domestic Insurance Market**

14. Guernsey commenced an industry consultation in late 2013 on a proposed revision of Regulations, Rules and Codes for licensed Insurers. The consultation paper included three proposed Risk Management Rules for insurers with accompanying notes:

- i. The insurer's Board is required to provide oversight in respect of the design and implementation of sound risk management and internal control systems and functions.
- ii. The insurer is required to establish, and operate within, effective systems of risk management and internal controls.
- iii. The insurer is required to have an effective risk management function capable of assisting the insurer to identify, assess, monitor, manage and report on its key risks in a timely way.

Research undertaken of Bermuda's insurance framework revealed no updates to the risk management measures for insurers since 2004.

### **F. SIGNIFICANT COSTS AND BENEFITS**

The costs associated with the issuance of the revised Rule will be dependent upon the existing practices of licensees and in particular its observance of the existing Rule issued in 2009. As the insurers have had sufficient time to implement the 2009 Rule, it is not anticipated that there will be significant costs incurred to implement the proposed amendments.

<b>Person</b>	<b>Costs</b>	<b>Benefits</b>
<b>Cayman Islands Monetary Authority</b>	<ol style="list-style-type: none"><li>1. Gazette and publication of new measure</li><li>2. Amend supervisory manuals</li><li>2. Training of Insurance Division staff</li></ol>	<ol style="list-style-type: none"><li>1. Enhance and support regulatory processes, in particular on-site inspection</li><li>2. Increases compliance with insurance core principles</li><li>3. Requires licensees to conduct own risk assessment, therefore increasing safety and decreasing probability of failure.</li></ol>

<b>Cayman Islands</b>	<p>None</p>	<ol style="list-style-type: none"> <li>1. Improved safety and soundness of insurers in the Cayman Islands by requiring insurers to have a comprehensive framework that should in turn reduce the negative financial effect for the industry of adverse exposure to these risks.</li> <li>2. Enhancement of the reputation of the Cayman Islands as a leading financial services centre overall with prudent and progressive regulation.</li> <li>3. Increased protection for policyholders due to the reduced risk of failure</li> </ol>
<b>Licensees</b>	<p><u>For licensees currently complying with the 2009 Rule:</u></p> <ol style="list-style-type: none"> <li>1. Amend their Risk Management Framework to include new elements (e.g. risk tolerance limits, identification of assumptions, control of fraud and money laundering risks)</li> <li>2. Implementing a plan to communicate risk management framework to key staff and staff training</li> <li>3. Implementing a feedback loop</li> <li>4. Requiring Board to approve outsourcing counterparties.</li> </ol> <p><u>For licensees not currently complying with the Rule:</u></p> <ol style="list-style-type: none"> <li>1. Implementation of policies and procedures on risk management as required by the Rule.</li> </ol>	<ol style="list-style-type: none"> <li>1. Better protection for policyholders as a result of the more robust management of risks to which their insurance companies are exposed.</li> <li>2. Provides information on the Authority's approach and sound business practice with regard to risk management, which in turn increases the reputation of the industry when conducting business with insurers outside the jurisdiction.</li> <li>3. Assists licensees in developing thorough risk management policies and procedures.</li> </ol>

## **G. COMMENTS AND CONSULTATION**

15. The Authority seeks consultation through written comments and representations concerning the proposed amendments to the Rule on "**Risk Management for Insurers**" from private sector associations.

16. The Authority must receive representations by **1700hrs on December 19, 2014.**

17. Comments and representations should be addressed to:

The Managing Director  
Cayman Islands Monetary Authority  
P.O. Box 10052 APO  
Grand Cayman KY1-1001,  
Cayman Islands, BWI  
Tel: 345-949-7089  
Fax: 345-945-1145  
Email: [consultation@cimoney.com.ky](mailto:consultation@cimoney.com.ky)  
and copied to [j.myles@cimoney.com.ky](mailto:j.myles@cimoney.com.ky)

18. The Authority shall have due regard to any representation made by private sector associations and industry stakeholders. The Authority shall provide a written response collating the feedback received and the Authority's position on this feedback. This response shall be copied to all relevant private sector associations only.