APPENDIX "B"

Cayman Islands Monetary Authority

PRIVATE SECTOR CONSULTATION

Rules and Statement of Guidance:
Actuarial Valuations

A. Introduction

1. Section 34(1)(a) of the Monetary Authority Law (2018 Revision) (as amended) ("MAL") states that –

   "*After private sector consultation and consultation with the Minister charged with responsibility for Financial Services, 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 Cayman Islands Monetary Authority ("the Authority") seeks consultation and comment from the private sector associations concerning the *Rules and Statement of Guidance - Actuarial Valuations* ("Rules and SoG").

B. Background/History

4. The International Association of Insurance Supervisors (IAIS) is the international body responsible for developing principles, standards and other supporting material for the supervision and regulation of the insurance sector. The IAIS published the revised Insurance Core Principles (ICPs) in 2011[1], which have been amended in subsequent years to reflect best practices. The ICPs set out the fundamentals of effective insurance supervision and seek to foster convergence towards a globally consistent supervisory framework.

5. The ICPs apply to insurance supervision internationally, however, there is scope for the tailoring of certain supervisory requirements, given differences in insurance markets across jurisdictions, particularly as it relates to complexity, nature and scale of insurance businesses. The ICP statements nonetheless, "*…prescribe the essential elements that must be present in the supervisory regime in order to promote a financially sound insurance sector and provide an adequate level of policyholder protection*"[2].

6. The legal bases for the actuarial report in the Cayman Islands are derived from the Insurance Law and supported by the requirements established in Form 4-G of the Insurance Reporting Regulations, 2013. The legislative approach is premised on ICP 14 which provides guidance for insurance supervisors on setting requirements for the valuation of assets and liabilities of insurers for solvency purposes.

7. In ensuring that the Cayman Islands' regulatory framework for insurance business is robust and aligned with international standards, CIMA established legal requirements for the submission of actuarial valuation reports. Section 9(1) of the Insurance Law establishes the requirements for insurers to submit a valuation report annually to the Authority as follows:

   > "*An insurer shall, except as otherwise approved by the Authority in writing and subject to subsection (3), submit to the Authority by way of annual return, within six months of the end of its financial year –*
   >
   > *… (b) an actuarial valuation of its assets and liabilities including loss and loss expense provisions, certified by an actuary approved by the Authority;…"*

8. Some insurers are exempted from the requirement to submit an actuarial valuation report as prescribed in section 9(3) of the Law, which states:

   > "*The following exemptions apply to the requirements of subsection (1) –*
   >
   > *(a) a class C insurer or a class B insurer that does not write long term business is not required to make submissions under subsection (1)(b) or (c); and*

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1 Updated in November, 2018.

2 *Insurance Core Principles*, International Association of Insurance Supervisors, 2015

(b) the Authority may in writing exempt other classes of insurer from the requirement under subsection (1)(b) where it considers it appropriate, based on the nature, scale or scope of the insurance business involved."

C. Purpose of Proposed Measure and Consistency with Authority's Functions

9. 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* …"

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

    i. endeavour to promote and enhance market confidence and the reputation of the Islands as a financial centre;
    ii. recognise the international character of financial services and markets and the necessity of maintaining the competitive position of the Islands, vis a 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;
    iii. 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
    iv. recognise the need for transparency and fairness on the part of the Authority.

11. The proposed *Rules and Statement of Guidance - Actuarial Valuations* will enhance the regulatory function of the Authority in line with Sections 6(1) and 6(3) of the MAL, as stated above.

D. International Standards

12. The ICPs prescribe the essential elements that must be present in the supervisory regime in order to promote a financially sound insurance sector and provide an adequate level of consumer protection. *ICP 14 – Valuation:*

    "…*considers the valuation requirements that should be met for the purpose of the solvency assessment of insurers within the context of IAIS risk-based solvency requirements that reflect a total balance sheet approach on an economic basis*[25] *and address all reasonably foreseeable and relevant risks*."[3]

    Table I highlights the ICP 14 standards which form the basis for the reporting expectations as it relates to actuarial valuations.[4]

Table I: ICP 14 Standards

14.1	The valuation addresses recognition, derecognition and measurement of assets and liabilities.

[3] *Insurance Core Principles*, International Association of Insurance Supervisors, 2015

[4] The Authority intends to issue more comprehensive guidance based the requirements of ICP 14, in the medium term.

14.2	The valuation of assets and liabilities is undertaken on consistent bases.
14.3	The valuation of assets and liabilities is undertaken in a reliable, decision useful and transparent manner.
14.4	The valuation of assets and liabilities is an economic valuation.
14.5	An economic valuation of assets and liabilities reflects the risk-adjusted present values of their cash flows.
14.6	The value of technical provisions and other liabilities does not reflect the insurer's own credit standing.
14.7	The valuation of technical provisions exceeds the Current Estimate by a margin (Margin over the Current Estimate or MOCE).
14.8	The Current Estimate reflects the expected present value of all relevant future cash flows that arise in fulfilling insurance obligations, using unbiased, current assumptions.
14.9	The MOCE reflects the inherent uncertainty related to all relevant future cash flows that arise in fulfilling insurance obligations over the full time horizon thereof.
14.10	The valuation of technical provisions allows for the time value of money. The supervisor establishes criteria for the determination of appropriate rates to be used in the discounting of technical provisions.
14.11	The supervisor requires the valuation of technical provisions to make appropriate allowance for embedded options and guarantees.

13. The establishment of a clear framework for conducting the valuation and for reporting of the results is a first step in complying with ICP 14. The rules and guidance will serve as a precursor to broader measures on the valuation of technical provisions for solvency purposes. The requirement to complete actuarial valuations is currently enshrined in the law and issuing the rules and guidance is important to ensure that the contents and quality are aligned with the expectations of the Authority and international best practice.

14. As it relates to international standards for actuarial work, the actuary is required to be a good standing member of a professional association. These associations typically serve as governing bodies for the profession and set standards for appropriate actuarial practice, including the preparation of reports. As such, it is expected that the valuation reports would be prepared and presented in compliance with the standards set by these respective professional bodies.

E. Jurisdictional Comparisons

15. Given that the majority of insurance regulators globally subscribe to the principles, standards and guidance established by the ICPs, many jurisdictions have established requirements for insurers to submit to the regulator, valuation reports prepared by an approved actuary. Additionally, jurisdictions in many cases, have issued measures to provide licensees with clear, minimum requirements for preparing the valuation reports, alongside guidance on the form and content of the reports. Consequently, the requirements for reporting of the actuarial opinion on the values of assets, liabilities and technical provisions of insurers, are in many cases, prescribed within

the regulatory and supervisory framework. Table II presents a summary of the requirements relating to the actuarial valuation reports in select jurisdictions.

Table II: Summary of Valuation Reporting Requirements

	Australia	**Bermuda**	**Canada**	**United States of America**	**Cayman Islands** *(proposed)*
Capital Assessment for Long Term Business	X	X	X	X	X
Assumptions and Limitations of Data	X	X	X	X	X
Stress Testing	X	X	X	X	X
Peer Review	X	X	X	X	X
Reinsurance Arrangements	X	X	X	X	X
Comparative Information	X	X	X	X	X

Australia

16. In June 2018, the Australian Prudential Regulation Authority (APRA) released revised, final prudential standards on actuarial and related matters that aim to assist actuaries to place greater focus on the most material matters relevant to their role, thereby better protecting the interests of the insurer they work for and its policyholders. The standards and guidelines relate to the preparation of the Financial Condition Report and Actuarial Valuation Report (AVR). As it relates to the AVR, the *Prudential Standard on Actuarial and Other Matters*, alongside other prudential standards, establishes requirements including the need to include a statement on the data and information relied upon; the methodologies and assumptions used and their related risks and limitation; and significant aspects of recent experience and the effect on the valuation.

Bermuda

17. In 2005, the Bermuda Monetary Authority (BMA) issued *Guidance Note #10: Role of the Approved Actuary*, which amongst other things, provides guidance on the preparation of the actuarial opinion. A new, updated guidance note was issued in

2017[5], and it sets out the expectations for the provision of formal professional opinions that are required on the insurance technical provision elements of the Economic Balance Sheet. The European wide Solvency II regime came into force from 1 January 2016 and the BMA has gained equivalence status with that regime. In respect of actuarial valuation reports, Solvency II leads to a highly prescriptive content for those reports which must at least follow through all the stages of the Solvency II regime.

Canada

18. The Office of the Superintendent of Financial Institutions issued the Guideline – *Appointed Actuary: Legal Requirements, Qualifications and Peer Review* in 2003, with revisions in 2006 and 2012. The Guideline describes the role of the actuary in federally regulated insurance companies and sets out some of the expectations with respect to that role, including the requirement to value the actuarial and other policy liabilities as at the end of a financial year. The valuation is required to be in accordance with accepted actuarial practice.

19. The Canadian Institute of Actuaries publishes extensive guidance material for actuaries in several areas affecting the valuation of insurance contract liabilities. The Institute's *Standards of Practice* includes a detailed section on reporting which establishes standards for the preparation of reports by actuaries including for presenting the description of the work, disclosure of assumptions, reservations, description and disclosures, the actuary's identification and reinsurance matters.

United States of America

20. The National Association of Insurance Commissioners (NAIC) sets out extensive guidelines for actuaries writing reports related to long-term business and to property and casualty business. The NAIC issued an amended Valuation Manual in August 2016. "*The Valuation Manual addresses the need to develop a valuation standard that enhances uniformity among the principle-based valuation requirements across states and insurance departments*." One of the goals for issuing the manual is to promote uniformity among states' valuation requirements by setting forth *inter alia*, the requirements for the actuarial opinion.

21. More generally, the Actuarial Standards Board sets standards for appropriate actuarial practice in the United States of America through the development and promulgation of Actuarial Standards of Practice (ASOP). The current fifty-four ASOPs describe the procedures an actuary should follow when performing actuarial services and identify what the actuary should disclose when communicating the results of those services.

F. Scope of Application and Rationale for Issuing Rules and SoG on Actuarial Valuations

22. As the Cayman Islands seek to maintain its standing as a world leading financial centre, alignment with international best practice is crucial. The establishment of a defined structure for reporting on actuarial valuations is a first step in complying with ICP 14. The Rules and SoG will serve as a precursor to broader guidance on the valuation of technical provisions for solvency purposes. The Authority intends to

[5] Actuary's Opinion on EBS Technical Provisions, Bermuda Monetary Authority, 2017.

review and establish a comprehensive framework based on the entire scope of requirements of the ICP, in the medium term.

23. The proposed Rules and SoG will help improve the quality and consistency of valuation report submissions and to ensure comprehensive assessments by actuaries. The measure provides additional guidance to insurers by clarifying the Authority's expectations about the content and reporting requirements for the reports.

24. The valuation report is expected to cover the insurance company's entire business and the actuary provides his/her opinion on the obligations arising out of insurance contracts. This opinion requires distinctions to be made and clarification to be provided based on the type of obligations accepted and the actuarial assumptions applied. The actuary is also expected to comment on the company's results from solvency testing and the extent to which the solvency requirements are being met based on current and future needs.

25. Discussion of the results of stress tests results are also a necessary part of the report, and the actuary should include the assumptions made for the stress testing exercises. Comparative information is also required, highlighting adjustments in assumptions, methodology and data, and the resultant effects on the opinion presented. The report should also contain statements about the quality of the underlying data sets.

26. The actuary is also required to highlight any risks that may pose a threat to solvency, including, but not limited to, underwriting, credit, market, operational and/or strategic risks. The impact of reinsurance arrangements should be included in the report, specifically, existing financial reinsurances and how they were treated in preparing the valuation.

G. Cost-Benefit Assessment of Implementing Rules and SoG on Actuarial Valuations

27. The relevant costs and benefits associated with the issuance of Rules and SoG are presented in Table III. Given that the measures only seek to document the minimum requirements and provide guidance and clarity to an existing legal obligation, it is not anticipated that there will be significant additional costs incurred to implement.

Table III: Costs and Benefits of Implementing Rules and SoG on Actuarial Valuations

	Costs	Benefits

	Costs	Benefits
CIMA	i. The Authority will incur administrative costs associated with the following: a. Gazetting and publishing of new measure; b. Conducting industry consultation; and c. Amending internal supervisory procedures documents. These costs are deemed to represent usual costs of the Authority carrying out its mandate. ii. With these new requirements, CIMA will need to dedicate staffing resources to conducting reviews and ensuring compliance with the newly established reporting requirements. Additionally, CIMA staff will need to be trained to perform the required reviews of the insurers' submissions.	i. CIMA will have more detailed and comprehensive insight into the balance sheet components (assets, liabilities and technical provisions) and risks of regulated insurers, where applicable. ii. Providing minimum standards to the industry on actuarial valuation reporting, will enable CIMA to be better able assess the condition and solvency position of licensees and therefore apply more appropriate remedial actions at an early stage. iii. CIMA will receive more consistent reports from insurers, which will facilitate more useful comparative analyses of the same insurer over varying periods; and across insurers.
Cayman Islands	i. There are no costs to the jurisdiction as a whole with the implementation of these requirements.	i. The implementation of rules and guidance for actuarial valuations for insurers will bode well for the jurisdiction as it relates to financial stability. Improved reporting allows for CIMA to make more comprehensive assessments of licensees and take prompt corrective actions to strengthen weak financial positions and avert failures and/or crises. ii. The jurisdiction will benefit from improved results from international assessments including the International Monetary Fund's Financial Sector Assessment Program[6] which is expected to be conducted in the Cayman Islands in the short to medium term.
Insurers	i. Insurers will bear the costs associated with the implementation of the new requirements, particularly as it relates to: a. Improving the actuarial review process, through for example,	i. Insurers will have more accurate information on the value of their assets, liabilities and technical provision, as applicable. ii. Early and more accurate detection of gaps, including asset or technical

6 For the insurance sector, the rating criteria are based on the degree of compliance with the ICP's.

	Costs	Benefits
	expanding data submissions; b. Amending internal policies and procedures documents; and c. Additional time and related costs for actuarial services. Notwithstanding, the measure is not expected to present significant additional costs for licensees as the requirement is not new.	provision shortfalls, will allow for improved ability of insurers to address issues and mitigate risks. iii. Improved clarity and consistency in the approach of insurers and their actuaries to the valuation reporting process. It is expected that over time insurers will benefit from time and resource savings due to greater clarity about the Authority's expectations for submissions of these reports.
Summary	Consequent to the above, it is determined that the benefits outweigh the costs and the issuance of the *Rules and Statement of Guidance- Actuarial Valuations* should be pursued by the Authority.	

H. Comments and Consultation

28. The Authority seeks consultation through written comments and representations from the private sector associations concerning the *Rules and Statement of Guidance - Actuarial Valuations.*

29. The Authority must receive representations by 21 June 2019.

30. Comments and representations must be addressed to:

The Managing Director
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Elizabethan Square
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With copy to: A.Glace@cimoney.com.ky

31. The Authority shall have due regard to any representation made by the 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.