

## **DRAFT – Changes are in bold print**

### REGULATION OF INSURANCE INDUSTRY ACT, NO. 43 OF 2000

Rules made by the Insurance Board of Sri Lanka under section 105 read with section 26 of the Regulation of Insurance Industry Act, No. 43 of 2000.

Chairman  
Insurance Board of Sri Lanka

**Colombo, ..... 2006**

#### RULES

1. These rules may be cited as Solvency Margin (General Insurance) **Amendment** Rules, **2006**.

2. (1) The amount of solvency margin, which is the difference between the value of the assets and the value of the liabilities, required to be maintained by any insurer who carries on general insurance business (in these Rules referred to as "insurer") shall be not less than the highest of the following:

(a) Rs. 50 million; or

(b) A sum equivalent to 20% of net **written** premium; or

(c) A sum equivalent to 40% of the average net outstanding claims for the three years immediately preceding the current year.

(2) The solvency margin referred to in paragraph (1) shall be maintained at all times during the year and, if required by the Board, be certified by the auditor.

3. The value of the liabilities of an insurer for the purpose of determining the solvency margin shall be:

(a) the technical reserve which includes :

(i) Net unearned premium reserve, which shall be computed on the basis of 1/365 method or 1/24 method. In the case of marine cargo insurance the 40% basis may also be used:

However for non-annual policies an insurer may, with the prior approval of the Board, adopt any other appropriate basis for calculation of unearned premium

reserve. The unearned premium reserve so calculated with reference to any of the above methods shall be adjusted for deferred acquisition expenses calculated on the same basis.

The insurer shall ensure that whatever the basis adopted is fully disclosed in the financial statements.

- (ii) Un-expired Risk Reserve, calculated on a net basis;
  - (iii) Reserve for net outstanding claims;
  - (iv) Reserve for incurred but not reported claims, calculated on a net basis; and
  - (v) Any other contingency reserves.
- (b) liabilities as shown in the Balance Sheet; and
- (c) any other liabilities of a special nature as notified by the Board.

**4. For the purpose of determining the solvency margin the following types of assets of the general insurance business in such amounts or percentages as specified below are regarded as admissible:**

<b>(a) (i) debt securities issued or fully guaranteed by the Government of Sri Lanka with a time to maturity not exceeding five (5) years;</b>	<b>100%</b>
<b>(ii) debt securities issued or fully guaranteed by the Government of Sri Lanka with a time to maturity exceeding five (5) years;</b>	<b>40%</b>
<b>(iii) debt securities issued or fully guaranteed by a Central Government or Central Bank of a country and carrying an investment grade rating;</b>	<b>20%</b>
<b>(iv) Accrued interest upto the date of calculation of the solvency margin on the above categories of investments. (A statement should be provided to the IBSL specifying the breakdown of the amount of interest accrued on each investment taken for solvency purposes)</b>	<b>Actual Amount</b>
<b>(b) Ordinary Shares of a company listed on a licensed stock</b>	<b>30%</b>

exchange;

**(c) (i) Corporate debts, including bonds, debentures, Commercial Papers, and other similar financial instruments, issued by a licensed commercial bank or a licensed specialised bank and carrying an investment grade rating; or backed by a guarantee issued by a licensed commercial bank, which has an investment grade rating or a licensed specialised bank, which has an investment grade rating or a Multilateral Agency; 60%**

**(ii) Corporate debts, including bonds, debentures, Commercial Papers, and other similar financial instruments which are listed on a licensed stock exchange; 10%**

**(iii) Corporate debts, including bonds, debentures, Commercial Papers, and other similar financial instruments, issued by a company and carrying an investment grade rating; 10%**

**(iv) Corporate debts, including bonds, debentures, Commercial Papers, and other similar financial instruments, issued by a company, which has an investment grade rating; 10%**

**(v) asset backed securities carrying an investment grade rating;**

**Note : The overall investment C (i) to C (v) should not exceed 60%.**

**(vi) Accrued interest upto the date of calculation of the solvency margin on the above categories of investments. (A statement should be provided to the IBSL specifying the breakdown of the amount of interest accrued on each investment taken for solvency purposes) Actual Amount**

**(d) (i) Deposits with licensed commercial banks or licensed specialised banks carrying an investment grade rating; 40%**

**(ii) Deposits with licensed finance companies carrying an investment grade rating; 10%**

**Note : The overall investment in d (i) to d (ii) should not exceed 40%.**

<b>(iii) Cash in hand (Physical cash &amp; cheques received);</b>	<b>10%[in all banks]</b>
<b>(e) freehold land and building (including the land value) occupied by the insurer;</b>	<b>10%</b>
<b>(f) freehold land and building (including the land value) held for investment purposes;</b>	<b>10%</b>
<b>(g) unit trusts/mutual funds;</b>	<b>25%</b>
<b>(h) gold;</b> <b>(Subject to the condition that the insurer takes all measures to keep the gold in safe custody in a bank recognized by the Board.)</b>	<b>20% or a higher percentage with the approval of the Board for which approval may be considered by the Board on a case by case basis based on the investment restrictions imposed on the insurer</b>
<b>(i) Investments made in all related companies;</b> <b>(The investments are required to be made in accordance to the limitations specified above)</b>	<b>7.5% subject to the maximum exposure, other than in licensed commercial banks or licensed specialized banks carrying an investment grade rating, being 5%.</b>
<b>(j) net amounts receivable for not more than six (6) months from re-insurers or ceding companies net of amount payable to same parties;</b>	<b>Actual amount</b>
<b>(k) premium outstanding for not more than 60 days from the inception of the policy;</b>	<b>Actual amount</b>

5. (1) The value of admissible assets under Rule 4 shall be determined in the following manner: -

**Asset categories specified in Rule 4 above**

**Valuation Methodology**

**4(a)(i),(ii), (iii)**

**shall be taken at cost as adjusted for amortisation of premiums or accretion of discounts, allocated on a systematic basis to maturity date using either the straight line method or constant yield method whichever is lower or any other method determined by the Board;**

**4(b)**

shall be valued at cost or at market value, whichever is lower;

**4(c)(i),(ii), (iii),(iv)**

**shall be taken at cost as adjusted for amortisation of premiums or accretion of discounts, allocated on a systematic basis to maturity date using either the straight line method or constant yield method whichever is lower or any other method determined by the Board;**

**4(c)(v)**

**shall be taken at cost as adjusted for amortisation of premiums or accretion of discounts, allocated on a systematic basis to maturity date using either the straight line method or constant yield method whichever is lower or any other method determined by the Board;**

**4(d)(i),(ii)**

**shall be the principal value of the deposit, plus the accrued interest;**

**the value of freehold land**

**shall be at cost value or at a re-valued amount determined by a valuer approved by the Board;**

**the value of freehold building**

**shall be at cost value less accumulated depreciation or at a re-valued amount determined by a valuer approved by the Board less accumulated amount of depreciation after such revaluation;**

**4(g)**

**shall be valued at, cost or managers buying price, whichever is lower;**

**4(h)**

shall be valued at cost or at market value, whichever is lower;

**4(j)**

shall be at the amount due after deducting the provision for bad and doubtful debts ; and

**4(k) shall be at an amount not exceeding the amount outstanding after deducting the provision for bad and doubtful debts, which are outstanding more than 60 days from the inception of the policies.**

**(2) Subject to the provisions of paragraphs 1 (k) of this Rule, an insurer shall provide for all balances, which are outstanding for more than six months from the due date of such balances, as a bad and doubtful debt.**

**(3) An insurer shall treat an investment income, which is overdue for more than six months, as a doubtful debt. The asset on which the investment income is derived shall be excluded in calculating the solvency margin.**

**(4) The revaluation of freehold land and building and the valuation of any admissible assets the manner of determination of which is not provided for in paragraph (1) of this Rule shall be carried out in accordance with the Sri Lanka Accounting Standards.**

**6. In the event an asset specified in Rule 4 (a)(iii), (c)(i), (c)(iii), (c)(iv), (c)(v), (d)(i) and (ii) above, is issued outside Sri Lanka or issued by an entity incorporated outside Sri Lanka, such asset is considered as admissible only if such asset is rated by a Credit Rating Agency listed in Part (I) of Table "A" below. If an asset specified in the above rules is issued in Sri Lanka or issued by an entity incorporated in Sri Lanka, such asset is considered as admissible only if such asset is rated by a Credit Rating Agency listed in Part II of Table A or by any other rated by a Credit Rating Agency registered by the Securities and Exchange Commission of Sri Lanka under the Securities and Exchange Commission Act, No. 36 of 1987.**

7. In any dispute arising due to the non-conformity with the requirements of Rule 3, a copy of the guidelines certified by the Board as the current applicable guidelines referred in that Rule, shall be admissible as evidence in any court of law and shall be regarded as a prima facie proof of the matters contained therein.

8. Where, on the date of the coming into operation of these Rules, an insurer who carries on general insurance business is maintaining a solvency margin of such amount determined in accordance with a method other than the method provided for in these Rules, such insurer shall be entitled, notwithstanding anything to the contrary in these Rules, to continue to use such method for a period not exceeding one year from the date of coming into operation of these Rules, and shall thereafter be required to comply with the provisions of these Rules.

9. In these Rules unless the context otherwise requires -

"Act" means the Regulation of Insurance Industry Act, No. 43 of 2000;

**"Asset backed Securities"** means a security that is primarily serviced by cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert in to cash within a finite time period plus any rights or other assets designed to assure the servicing or timely distribution of proceeds to the security holders;

**"Board"** means the Insurance Board of Sri Lanka, established under the provisions of the Regulation of Insurance Industry Act No. 43 of 2000;

**"Equity"** includes the issued share capital and reserves;

**"investment grade rating"** means a credit rating assigned by the corresponding credit rating agency set out in Part (I) and Part (II) of Table "A" below or any better credit rating assigned by such credit rating agency; or a credit rating which indicates similar credit quality as set out in Part (II) of table "A" below, assigned by an entity registered by the Securities and Exchange Commission of Sri Lanka under the Securities and Exchange Commission Act, No. 36 of 1987; To be applicable, the ratings should have been assigned or reviewed within the preceding eighteen months;

**"issued shares"** means the subscribed and the paid up share capital;

**"licensed commercial bank", "licensed specialised bank" and "licensed finance company"** shall be institutions licensed by a Government Authority to carryon such business;

**"licensed stock exchange"** means a stock exchange licensed by a Government Authority;

**"Multilateral Agency"** means and includes the International Finance Corporation and any other similar institution that may be considered and approved by the Board as a Multilateral Agency from time to time;

**"Related company"** shall have the same meaning given to it under the Sri Lanka Accounting Standards;

**"technical reserve"** means the technical reserve maintained under section 24 of the Act and includes:-

(i) Net unearned premium reserve, which shall be computed on the basis of 1/365 method or 1/24 method. In the case of marine cargo insurance the 40% basis may also be used:

However for non-annual policies an insurer may, with the prior approval of the Board, adopt any other appropriate basis for calculation of unearned premium reserve. The unearned premium reserve so calculated with reference to any of the above methods shall be adjusted for deferred acquisition expenses calculated on the same basis.

The insurer shall ensure that whatever the basis adopted is fully disclosed in the financial statements.

(ii) Un-expired Risk Reserve, calculated on a net basis;

(iii) Reserve for net outstanding claims;

(iv) Reserve for incurred but not reported claims, calculated on a net basis; and

(v) Any other contingency reserves.

(b) liabilities as shown in the Balance Sheet; and

(c) any other liabilities of a special nature as notified by the Board.

"unit trusts" or "mutual funds" mean and include unit trusts or mutual funds regulated by a Government Authority.

**Table A**

**INVESTMENT GRADE CREDIT RATINGS  
(Part I)**

<b>CREDIT RATING AGENCY</b>	<b>RATING OF ENTITY OR SECURITY</b>	<b>SHORT TERM (LESS THAN ONE YEAR) RATING OF SECURITY</b>
<b>(1) Moody's Investor Services</b>	<b>Baa3</b>	<b>P3</b>
<b>(2) Standard and Poor's Corporation</b>	<b>BBB-</b>	<b>A3</b>
<b>(3) Fitch Ratings</b>	<b>BBB-</b>	<b>F3</b>
<b>(4) A. M. Best Company, Inc.</b>	<b>bbb-</b>	<b>AMB-3</b>

(Part II)

<b>CREDIT RATING AGENCY</b>	<b>RATING OF ENTITY OR SECURITY</b>	<b>SHORT TERM (LESS THAN ONE YEAR) RATING OF SECURITY</b>
<b>(1) Fitch Ratings (Lanka) Ltd.</b>	<b>BBB-(sri)</b>	<b>F3 (sri)</b>
<b>(2) Lanka Ratings</b>	<b>BBB3</b>	<b>L-3</b>