

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 / Director General,
Insurance Board of Sri Lanka

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

RULES

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

2. These rules will not apply to investment linked long-term products.

3. (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 long term insurance business (in these Rules referred to as "insurer") shall be not less than five per centum of the value of the liabilities of such insurer as determined in the manner provided for in these Rules.

(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 appointed actuary.

4. The value of the liabilities of an insurer for the purpose of determining the solvency margin shall be made in accordance with the currently applicable guidelines of an entity designated by the Board and be subject further to the following:

(a) the liabilities in respect of a long term insurance policy shall be equal to the amount, if any, by which the present value as at the date of valuation, of the benefits payable, exceeds the present value as at the date of valuation of the adjusted premium, if any, payable after such date;

(b) where a part or the whole of the premium payable under a long term insurance policy is accumulated in a participating or nonparticipating fund to be paid as a benefit either on maturity of the policy or on the death of the life insured, the present value of the fund as at the date of the valuation determined on the actuarial basis specified in Rules **8 and 9** of these Rules, shall be deemed to be the liability under the policy corresponding to the accumulated portion of the

premium and the liability in respect of any portion of the premium which is utilised to cover the contingency of death or survival as an extension to the policy, shall be determined in accordance with the manner specified in paragraph (a);

(c) where the benefit payable under a long term insurance policy is the accumulated amount of the premiums paid at a guaranteed rate of interest, the accumulated amount as at the date of valuation shall be deemed to be the liability under the policy and any other liability in addition to the accumulated amount, shall be determined in accordance with the manner specified in paragraph (a).

5. For purpose of paragraph (a) of Rule **4**, the adjusted premium payable after the date of valuation will be the actual value of the premium, adjusted by assuming that the policy provides only for such premiums as are sufficient to provide for the risk incurred by the insurer in issuing the policy, without provision for bonuses, office expenses or any other charges, and by making further adjustments as provided for in paragraph (a) or (b) of Rule **6**, whichever will produce the lower adjusted value.

6. The further adjustments referred to in Rule **5** shall consist of -

(a) assuming that the policy is issued one year after the date of its issue, but without postponing the time when the premium ceases or policy money becomes payable if that time is fixed by reference to the date of issue, and to calculate the premium referred to in Rule **5** accordingly; or

(b) adding to the premium referred to in Rule **5**, such amount as would have at the date of issue of the policy, a capitalized value equal to four per centum of the basic sum assured, taking any annuity at the capitalised value it would have on becoming payable.

7. Notwithstanding the provisions of Rule **5 and Rule 6**, the adjusted value of the premium shall not be more than ninety per centum of office premium payable under the policy.

8. An actuary shall determine the value of the liabilities of an insurer by using -

(a) such mortality tables issued by an entity designated by the Board under Rule **4** above; or

(b) any other mortality table producing a solvency margin less than the solvency margin produced by the tables referred to in paragraph (a), which is approved by the Board for such purpose.

9. In determining the value of the liabilities of an insurer, an actuary shall use a rate of interest as specified below:-

(a) for valuing participating non-single premium long term insurance policies, a rate of interest not exceeding the highest of the following, subject to an upper limit of eight per centum per annum:-

(i) five per centum per annum;

(ii) sixty-five per centum of the average of the annual net of tax return on the Long Term Insurance Fund during the preceding three years from the date of valuation, if tax has been actually paid; or

(iii) fifty-five per centum of the average gross return, before paying tax on the Long Term Insurance Fund during the preceding three years from the date of valuation;

Provided that, where an insurer has commenced operations within the last three years preceding the date of valuation, the rate of interest to be used shall be the rate specified in subparagraph (i) of this paragraph;

(b) for valuing participating single premium long term insurance policies, one and half per centum per annum more than the rate determined in accordance with the manner specified in paragraph (a);

(c) for valuing non-participating non-single premium long term insurance policies, including paid up policies which do not participate in future bonus, one and half per centum per annum more than the rate determined in accordance with the manner specified in paragraph (a);

(d) for valuing non-participating single premium long term insurance policies, three per centum per annum more than the rate determined in accordance with the manner specified in paragraph (a);

(e) for valuing simple reversionary bonus of participating long term insurance policies, one and a half per centum per annum more than the rate determined in accordance with the manner specified in paragraph (a).

10. An extension to a long term insurance policy covering contingency of death or survival shall be valued by an appointed actuary in accordance with the requirements specified in Rule **4 to 9** of these Rules.

11. It shall be the duty of an actuary to provide an appropriate reserve and state the basis of such reserving, in respect of -

- (a) the immediate payment of claims;
- (b) in the case of limited payment policies and paid up policies, the future expenses and bonuses;
- (c) liabilities existing or which may arise in the future, in respect of policies which have lapsed and which were not included in the valuation;
- (d) disability benefits in payment as a result of the disability of the life insured;
- (e) policies kept in force, where the premiums have been waived;
- (f) provision of benefits upon occurrence of the life insured's disability or the waiver of premiums in the future;
- (g) policy insuring a substandard risk or a high risk occupation; and
- (h) any other liability or contingent liability under long term insurance policies or extension of such policies.

12. Where the surrender value in the aggregate of the policies in force exceeds the value of the liabilities, an actuary shall determine the value of the liability at an amount not less than such aggregate surrender value.

13. Where a policy or an extension of a policy is treated as an asset, an actuary shall make the necessary adjustment to eliminate such asset value from the value of the liabilities.

14. Investment of monies lying to the credit of the Long Term Insurance Fund in the following types of assets **and** in such percentages **of the Long Term Insurance Fund** or amounts as specified below, are regarded as admissible:-

(a) (i) debt securities issued or fully guaranteed by the Government of Sri Lanka with a time to maturity not exceeding five (5) years;	100%
(ii) debt securities issued or fully guaranteed by the Government of Sri Lanka with a time to maturity exceeding five (5) years;	75%
(iii) debt securities issued or fully guaranteed by a Central Government or Central Bank of a country and carrying an investment grade rating;	20%
(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)	Actual Amount
(b) Ordinary Shares of a company listed on a licensed stock exchange;	40%
(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;	50%
(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; 10%

Note : The overall investment in c (i) to C (v) should not exceed 50%.

(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%.

(iii) Cash in hand (Physical cash & cheques received); 10%[in all banks]

(e) freehold land and building (including the land value) occupied by the insurer; 15%

(f) freehold land and building (including the land value) held for investment purposes; 15%

(g) unit trusts/mutual funds; 25%

<p>(h) gold; (Subject to the condition that the insurer takes all measurers to keep the gold in safe custody in a bank recognized by the Board.)</p>	<p>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</p>
<p>(i) Investments made in all related companies; (The investments are required to be made in accordance to the limitations specified above)</p>	<p>7.5% subject to the maximum exposure, other than in licensed commercial banks or licensed specialized banks carrying an investment grade rating, being 5% .</p>
<p>(j) outstanding policy loans</p>	<p>Actual amount</p>
<p>(k) outstanding mortgage loans on immovable properties of policyholders</p>	<p>10%</p>
<p>(l) net amounts receivable for not more than six (6) months from re-insurers or ceding companies net of amount payable to same parties;</p>	<p>Actual amount</p>

15. (1) The value of admissible assets under Rule **14**, shall be determined in the following manner :-

<p>Asset categories specified in</p>	<p>Valuation Methodology</p>
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**Rule 14
above**

**14(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;

14(b)

shall be valued at cost; at market value; or **any other method as determined by the Board**, whichever is lower;

**14(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;

14(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;

14(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;

14(g)

shall be valued at, cost; at managers buying price; or any other method as determined by the Board, whichever is lower;

14(h)

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

14(j)

shall not exceed the outstanding capital or the net realisable value of the

loan, whichever is lower; and

14(I) shall be at the amount due after deducting the provision for bad and doubtful debts.

(2) Notwithstanding the provisions of paragraphs (1) (I) 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 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 or leasehold 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.

16. In any dispute arising due to the non-conformity with the requirements of Rule 4, a copy of the guidelines certified by an entity designated by the Board under that Rule as the current applicable Guidelines referred to therein, shall be admissible as evidence in any court of law and shall be regarded as prima facie proof of the matters contained therein.

17. In the event an asset specified in Rule 14(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 or by any other Credit Rating Agency registered by the Securities and Exchange Commission of Sri Lanka under the Securities and Exchange Commission Act, No. 36 of 1987.

18. An insurer who carries on long term insurance business shall be entitled, notwithstanding anything to the contrary in these Rules, to maintain, from the date of the coming into operation of these Rules a Solvency Margin of three per centum in the first year, four per centum in the second Year, five per centum in the third year, determined in accordance with these Rules, and shall thereafter be required to comply with the provisions of these Rules.

Provided that where, on the date of the coming into operation of these Rules, an insurer who carries on long term 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 may with the approval of the Board 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.

19. In these Rules unless the context otherwise requires -

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

"Actuary" means an Actuary recognized under this Act;

"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 carry on such business;

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

“Long term insurance fund” for the purpose of this determination includes the policy holder's monies which is represented by an amount equal to the amount of liabilities in respect of all policies for which there exists a liability plus the amount of outstanding claims plus reinsurances accepted less reinsurances ceded, and also any amount of solvency margin that is required to be maintained from the shareholders' funds. It also includes any undistributed surplus.

“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;

“office premium” means the premium payable under the policy for the benefits being valued excluding extra premiums if any; and

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

“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)**

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

(Part II)

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

Designations by the Board under the Solvency Margin Rules (Long Term Insurance)

Rule 4

For the Purpose of Rule 4 the Guide Lines for the purpose of determining the value of the liabilities of an insurer for purpose of solvency margin shall be the currently applicable guidelines issued by the Institute of Actuaries in England.

Rule 8

For the purpose of Rule 8 the value of the liabilities of an insurer shall be determined by using the following tables, which are issued by the Institute of Actuaries in England:

- (a) the English Assured Lives Mortality Table A67/70 (ultimate) for valuing life insurance policies;
- (b) the (90)(m) ultimate table for valuing annuities on male lives; and
- (c) the (90)(f) ultimate table for valuing annuities on female lives.