FINANCIAL SERVICES
COMMISSION

GUIDELINE NO. 5

GUIDELINE ON ASSET AND LIABILITY VALUATION

(This guideline is issued pursuant to section 53 of the Financial Services Commission Act, on March 1, 2013)

ASSET AND LIABILITY VALUATION FOR SOLVENCY AND STATUTORY FUND CALCULATION

1.0 INTRODUCTION

1.1 Generally accepted accounting principles are acceptable methodologies for the preparation of general purpose financial reports of insurance companies. However, in instances of regulatory reporting requirements, there may be situations where the technical application of assets and liabilities for purpose of solvency and statutory requirements present a need for a variance in the presentation of the assets or the liabilities to appropriately monitor the risk of an insurance company. Any differences between the presentation of technical provisions for general purpose financial reports and published statutory filing reports should be explained and reconciled in terms of differences in data, discount rate, methodology and assumptions used together with the rationale for why any different approach is appropriate for solvency or statutory purposes. This note sets out the guidance for valuation of assets and liabilities where the statutory reporting requirements may differ from generally accepted accounting principles.

1.2 The Commission recognizes the need for clarity as to the scope and implementation of the provisions of the guideline if the regulatory system is to command the confidence of insurers and policyholders. It seeks, therefore, to ensure that those licensees operating in Barbados have a good understanding of the nature of the requirements and of the Commission's approach in implementing the Act, the regulations, and the guidelines which are associated.

1.3 The Commission's approach to the supervision of insurance is becoming increasingly risk-based. This means that the Commission, to the extent possible, identifies, assesses, prioritizes, and minimizes the likelihood of events or circumstances occurring with might prevent the Commission from achieving its objectives. Further to this the Commission assesses the risks posed by an insurer by gaining an understanding of a licensed insurer's operations, the risks it faces and how it deals with these risks. The consideration of the governance and the decision-making and control processes of an insurer is a key component of this assessment process. This approach to supervision is in contrast to a transaction-oriented review.

1.4 The Commission's guidance is of general application. There is likely to be a need for the Guideline to be revised and developed over time. Material changes in the Guidance will be published, generally through the issue of a revised version and communicated to the industry accordingly.

1.5 The guideline is not intended to be exhaustive. Any guidance provided is intended to be reflective of minimum standards that should be observed in all cases. In any areas where guidance is not specific, licensees should be guided by the Guidance's underlying spirit. Licensees must take the appropriate steps to become compliant with the guideline.

2.0 DEFINITIONS

2.1 ***Solvency requirements*** for licensees are detailed under the Insurance Act Cap 310 for domestic insurance companies and under the Exempt Insurance Act Cap 308B for off shore insurance companies.

2.2 ***Statutory Deposit*** is the deposit requirement as detailed under Section 23 of the Insurance Act Cap 310.

2.3 ***Statutory Fund*** is the fund requirement as detailed under Section 25 of the Insurance Act Cap 310.

3.0 TO WHO DOES THIS GUIDELINE APPLY

3.1 This guidance applies to all insurers and intermediaries licensed to write insurance policies under the FSC Act, the Insurance Act Cap310 and the Exempt Insurance Act CAP308B.

4.0 GENERAL PROVISIONS

4.1 The context and purpose of the valuation of assets or liabilities of an insurer are key factors in determining the values that should be placed on them. Assets and liabilities should be recognised and derecognised to the extent necessary for insurance specific risks to be appropriately recognised.

4.2 Solvency assessment based on consistent valuation of assets and liabilities is a prerequisite for obtaining a meaningful insight into the asset-liability positions of an insurer and an understanding of the financial position of an insurer relative to other insurers. Therefore it is very important that when monitoring the solvency margin and statutory fund and deposit levels of all insurance companies licensed under the relevant acts that the regulator be confident that the value of assets being presented in the statutory filings are being done so using the same methodologies by all insurance companies. Having this standard will enable reliable information on which to base the actions that are taken by insurers and their supervisors in respect of those positions.

4.3 Undertaking valuation on consistent bases means that differences in values of assets and liabilities can be explained in terms of the differences in the nature of the cash flows including their timing, amount and inherent uncertainty, rather than differences in methodology or assumptions.

5.0 TECHNICAL PROVISIONS

Valuation of Liabilities

5.1 With respect to the valuation of liabilities presented by the insurance companies, the Commission would expect that general liabilities are presented using generally accepted accounting principles and that the values are verified by an auditor.

5.2 With respect to technical insurance liabilities including;

5.2.1 Provisions for claims
5.2.1 Provisions for claims incurred but not reported (IBNR), and
5.2.1 Provisions for unearned premiums and unexpired risks

The Commission would expect that the liability values presented in this regard are done so using established actuarial methodologies for both general insurance business and long term insurance business. The technical liabilities should be reported showing the gross liabilities, the estimate for reinsurance recoverable, and the net liabilities. The Board of Directors and Senior Management of insurance companies should ensure that this is being done and that the rationale being used to estimate the technical liabilities is disclosed in the notes of the financial statements.

5.3 In addition, Section 43 (1) of the Insurance Act Cap 310 and Section 18 (3) of the Exempt Insurance Act Cap 308B as listed below require that companies writing long term insurance business present an actuarial confirmation of the value of the liabilities.

43. *(1) Every insurance company that carries on long-term business shall, not less than once annually or for such other period as the Supervisor may allow but not exceeding 3 years, cause a review of the company's operations to be carried out by an actuary, including a valuation of its liabilities.*

18. *(3) A licensee engaged in long-term insurance business shall, in addition, submit to the Supervisor a certificate of an actuary approved by the Supervisor stating that the licensee's reserves have been established in accordance with accepted actuarial standards*

5.4 The Commission expects that all licensees follow the actuarial requirements as outlined in the relevant sections of the respective Act as a minimum standard for presenting technical insurance liabilities.

Valuation of Assets

5.5 Statutory Fund Assets – Section 33 (1) of the Insurance Act Cap 310 states that *"statutory fund shall not be invested except in the securities specified in the Second Schedule"* and any assets held in trust for the statutory fund must therefore confirm to the restrictions contained therein.

5.6 The assets declared in the statutory fund shall be entered into the fund using the following valuation methods:

5.6.1 **Bonds and Debentures** – Entered at Face Value or fair market value with a note on the methodology used in the fair value calculation.

5.6.2 **Cash** – Entered at Face Value

5.6.3 **Securities, Shares, Preferred Shares, and Stocks** – Entered at fair market value. If stocks are not traded on a public stock exchange, the financials should contain a note about the valuation method used to determine the fair market value and also a declaration should be made about any discount rate used in the valuations.

5.6.4 **Real estate** – Entered at fair market value. An updated real estate valuation prepared by a real estate valuer licensed in Barbados should be presented at least once every three years. The Commission reserves the right to request a real estate valuation more frequently in circumstances where it is deemed necessary. If the valuation is requested more frequently the Commission shall notify the insurer of the reason for the request.

5.6.5 **Mortgages** – Presented at amortized value annually when the trustee confirms the assets in the statutory fund.

5.6.6 **Any other asset allowed in the second schedule of the Act and not described above** – Presented at fair market value with a note detailing the methodology used for valuation.

5.7 Statutory Deposit Assets – Section 23 (4) of the Insurance Act Cap 310 states that *"Any deposit made under this section may be either in the form of cash or in the form of prescribed securities or partly in cash and partly in prescribed securities."* The prescribed securities allowable as per the Prescribed Securities Regulations are as follows:

5.7.1 Securities of the Government of Barbados;

5.7.2 Securities of the government of any part of the Commonwealth other than Barbados, up to a limit of 20%;

5.7.3 Securities of the government of the United States of America or any other country approved by the Minister, up to a limit of 20%.

(a) **The prescribed securities listed in the statutory deposited should be entered at face value**.

(b) **Cash amounts should be entered at face value**

6.0 COMPLIANCE

6.1 Compliance with this Guidance will be checked by the Commission on an on-going basis as the Commission conducts it's off site review of the statutory filings of insurance companies and as such the Commission expects that all licensees will comply fully with the contents of this guideline. Companies will be granted a phase-in period of 1 year from the date of the guideline to become compliant.