

Notice No: MAS 208
Issue Date: 28 August 2004

This Notice replaces MAS 208 dated 18 August 1999.

NOTICE ON FINANCIAL REINSURANCE

Introduction

1. This Notice is issued pursuant to section 64(2) of the Insurance Act (Cap. 142) (“the Act”). It comprises both mandatory requirements (Part I) and guidelines (Part II).
2. This Notice shall be read in conjunction with the provisions of the Act and the Insurance (Valuation and Capital) Regulations (G.N. No. S498 /2004) (“the Regulations”).
3. This Notice applies to any insurer registered to carry on general business.
4.
 - (a) With effect from 28 August 2004, MAS Notice 208 on “Financial Reinsurance” dated 18 Aug 1999 shall be cancelled and this Notice shall come into force.
 - (b) This Notice shall not apply to any registered insurer which carried on general business immediately before 23 August 2004 for the period from 23 August 2004 to 31 December 2004.
 - (c) The insurer referred to in sub-paragraph (b) shall continue to comply with MAS Notice 208 dated 18 Aug 1999 in force immediately before 28 August 2004 during –
 - (i) the period referred to in sub-paragraph (b); and
 - (ii) the period from the day immediately following the end of the period referred to in sub-paragraph (b) to the day on which the registered insurer lodges the statements of account and other statements required under the Insurance (Accounts and Statements) Regulations (Rg 2) in force immediately before 23 August 2004 in respect of the accounting period beginning 1 January 2004 and ending on 31 December 2004 (both days inclusive),

for the purpose of enabling the insurer to comply with regulation 18(2) of the Insurance (Accounts and Statements) Regulations 2004 (G.N. No. S 494/2004) in respect of the preparation and lodgment of the statements of account and other statements required to be lodged under the Insurance (Accounts and Statements) Regulations.
 - (d) Notwithstanding sub-paragraphs (b) and (c), where a registered insurer has made an election under regulation 24(3) of the Regulations –
 - (i) sub-paragraph (b) shall not apply to the insurer from the date the election is made; and

- (ii) sub-paragraph (c) shall continue to apply to the insurer.

Definition

5. For the purpose of this Notice:

- (a) Due to the diversity of the types of financial reinsurance, sometimes referred to as "finite risk reinsurance", it is difficult to have a prescriptive definition for the term "financial reinsurance contract". In general, a "financial reinsurance contract" may be distinguished by some or all of the following characteristics:
 - (i) multi-year contract term, except for cases that follow the expiry of original policies;
 - (ii) retrospective provisions that give the contracting parties future rights and obligations as a result of past events, where premiums, commissions or commutation agreements depends, or depend in part, on the timing and amount of claims payments;
 - (iii) premiums are determined taking into account the future (expected) investment income;
 - (iv) the financial outcome of the contracts, including the effect on the profit of both parties, can be predicted with some certainty at the outset, that is, variability of outcome is reduced; and
 - (v) combined coverage for assets (investment) risks and liability (insurance) risks;
- (b) "experience account" means record of amounts payable by the cedant to the reinsurer under a reinsurance contract; and
- (c) "reinsurance management strategy" means a plan for ensuring clear assignment of responsibility and control of reinsurance arrangements, where a portion of the risks assumed by an insurer is ceded to another insurer.

Part I – Mandatory Requirements

Prudent Management Oversight

- 6. An insurer shall exercise prudent management oversight and implement adequate controls in respect of the transactions relating to financial reinsurance contracts. In the formulation of financial reinsurance contracts, there shall be clear documentation on the considerations relating to:
 - (a) the selection of counterparty;
 - (b) the protection of policyholders' interest; and

- (c) the evaluation of the benefits to be derived under the financial reinsurance contract.
- 7. Prior to its entry into any financial reinsurance contracts, an insurer shall develop and implement a reinsurance management strategy approved by its Board of Directors, and shall maintain such reinsurance management strategy until the insurer ceases to be a party to any financial reinsurance contract.
- 8. An insurer shall ensure that its entry into any financial reinsurance contract is consistent with its reinsurance management strategy. A direct insurer shall give reasonable prior notice to its Board of Directors of any intention to enter into, or to effect or permit any material change in the terms of, any financial reinsurance contract transactions.

Accounting Treatment

- 9. A financial reinsurance contract that satisfies the condition of significant risk transfer (as determined in accordance with paragraphs 20 to 22 below) shall be accounted for as a contract of reinsurance by both the cedant and assuming insurer in the Forms 1, 2 and 6 required to be prepared and lodged with the Authority under the Insurance (Accounts and Statements) Regulations (G.N. No. S 494 /2004).
- 10. A financial reinsurance contract that does not satisfy the condition of significant risk transfer shall be treated as a deposit by both the cedant and assuming insurer. That is, amounts in respect of such a contract shall be excluded from Forms 2 and 6.

For Financial Reinsurance Contracts that Satisfy the Condition of Significant Risk Transfer

Disclosure and Reporting for General Business Ceded

- 11. The cedant shall lodge with the Authority, as notes to Form 1, the following information relating to the financial reinsurance contracts:
 - (a) the amount of reinsurance premiums payable and any additional payments accrued under the experience account, to be included under “amounts owing to insurers”;
 - (b) the amount of recoveries receivable, to be included under “reinsurance recoverables”; and
 - (c) any other amounts receivable from reinsurers, such as profit commissions or refunds accrued under the experience account, to be included under “other assets”.
- 12. Subject to paragraph 13 below, where a financial reinsurance contract has been entered into or modified during an accounting period, and in which general business has been ceded by an insurer under the financial reinsurance contract, the insurer shall lodge with the Authority, as notes to Form 6, a

statement containing the following information in respect of the financial reinsurance contract:

- (a) the type of business covered or a description of the risks covered if it involves only part of a business category;
 - (b) the type of cover, including such details of the terms and conditions of the contract as are necessary for a proper understanding of the nature of the cover;
 - (c) details of any limits on cover as are necessary for a proper understanding of the contract, including any event limits, limits on the amount of business ceded, limits on the number of reinstatements and aggregate limits; and
 - (d) the period of cover.
13. Where a financial reinsurance contract is entered into by an insurer during an accounting period and modified during another accounting period, the information contained in the statement to be lodged in respect of the second-mentioned accounting period pursuant to paragraph 12 above shall be limited to the changes to the information previously lodged.
14. The cedant shall lodge with the Authority, as notes to Form 6, the following information relating to financial reinsurance contracts:
- (a) the amount of premiums ceded, including any additional payments accrued under the experience account, which shall be included under “reinsurance business ceded”;
 - (b) the amount of recoveries, which shall be included under “recoveries from reinsurance business ceded”; and
 - (c) the amount of reinsurance commissions received or receivable, including profit commissions or any form of refunds accrued under the experience account, which shall be included under “reinsurance commissions”.

Disclosure and Reporting for General Business Assumed

15. In completing Form 1, amounts relating to a financial reinsurance contract shall be reported by the assuming insurer as follows:
- (a) amounts owing to cedants, including recoveries, commissions, profit commissions or refunds, shall be included as “amounts owing to insurers”;
 - (b) premiums receivable from cedants shall be included as “outstanding premiums and agents’ balances”; and
 - (c) any additional payments accrued and receivable from cedants under the experience account shall be included as “other assets”.

16. For a financial reinsurance contract entered into or modified during the accounting period, the assuming insurer shall disclose, as notes to Form 6, the total reinsurance premiums written, which shall be included under "reinsurance business accepted".

For Financial Reinsurance Contracts that Do NOT Satisfy the Condition of Significant Risk Transfer

17. Where amounts in respect of a financial reinsurance contract that does not satisfy the condition of significant risk transfer have been excluded from Forms 2 and 6, the following information shall be disclosed by both the cedant and assuming insurer as notes to Form 1:
- (a) a description of the terms of that contract;
 - (b) a description of the accounting treatment adopted and an explanation for adopting that treatment;
 - (c) a statement of the amounts paid and received during the accounting period under that contract; and
 - (d) a statement of the amounts in respect of the contract included in Form 1.
18. An insurer may elect to show the information required pursuant to paragraph 17 above in respect of groups of contracts that were effected in the same financial year with substantially the same contract terms and in respect of which the same accounting treatment has been adopted.

Part II – Guidelines

Risk Transfer

19. An insurer is advised to use financial reinsurance arrangements that involve elements of insurance risk transfer.
20. A significant insurance risk transfer is deemed to have taken place under a contract of reinsurance when the following conditions are satisfied:
- (a) it is reasonably possible that the assuming insurer may realise a significant loss from the contract; and
 - (b) it is reasonably possible to have a significant range of outcomes under the contract.
21. Whether or not a insurance risk transfer is "significant" should be assessed in the context of the commercial substance of the contract or, where there are significant connections among a series of contracts, such contracts being evaluated as a whole, and should be judged with reference to the range of outcomes that would reasonably be expected to occur in practice.

22. The assessment as to whether insurance risk is transferred should be made prospectively, at the time the contract is entered into.

Contravention of requirements imposed

23. Contravention of any requirement imposed under Part I of this Notice shall be an offence and shall attract the penalty specified in section 55(2) of the Act.