

## **RESPONSE TO FEEDBACK RECEIVED – SECOND CONSULTATION PAPER ON POLICY OWNERS’ PROTECTION FUND (“PPF”)**

### **1 Introduction**

1.1 In December 2009, the Monetary Authority of Singapore (“MAS”) conducted a second consultation on PPF. The PPF seeks to compensate policy owners in the event of default of their insurers.

1.2 The consultation period closed on 29 January 2010. Various parties commented on the consultation paper and MAS would like to thank all respondents for their contributions. The respondents are listed in Annex 1.

1.3 We have carefully considered the feedback received and incorporated the relevant feedback into the review of PPF. Comments that are of general interest, together with MAS’ responses, are set out below.

### **2 Increase in Level of Coverage from 90% to 100%**

2.1 The second consultation paper proposed to increase the coverage under the PPF life and general insurance schemes from 90% to 100% of protected liabilities of all life and accident and health (“A&H”) policies, and all protected general insurance lines<sup>1</sup> (instead of only compulsory insurance policies<sup>2</sup>), respectively. Some respondents felt that the level of

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<sup>1</sup> The proposed general insurance lines to be covered under the PPF general insurance scheme are:

- (i) Motor third party liability injury insurance;
- (ii) Work Injury Compensation Act liability insurance;
- (iii) Personal motor insurance;
- (iv) Individual and group A&H insurance;
- (v) Personal property (structure and contents) insurance;
- (vi) Foreign domestic maid insurance; and
- (vii) Personal travel insurance.

<sup>2</sup> “Compulsory insurance policies” is defined in the Insurance Act as any policy or security which satisfies the requirements of the Motor Vehicles (Third Party Risks and Compensation) Act (Cap 189) or the Work Injury Compensation Act (Cap 354).

coverage for all life, A&H and non-compulsory insurance policies should remain at 90%, as proposed in the first consultation paper of December 2005, to minimise moral hazard. They were concerned that by moving to 100% coverage, consumers would not exercise care in their selection of their insurers and might place less emphasis on the financial soundness of their insurers given the safety net.

### MAS' Response

2.2 The proposed increase in the level of coverage to 100% is to allay the concerns of policy owners, should they become anxious with rumours of a potential failure of an insurer and seek to cancel their policies, which may be to their detriment. Where the level of coverage is only 90%, policy owners may perceive that they may be better off getting back 100% of their policies' surrender values, rather than waiting for the Singapore Deposit Insurance Corporation ("SDIC") to make the necessary payout after the PPF has been triggered. If the insurer does not fail, policy owners who prematurely surrender their policies may not be able to obtain equivalent new insurance cover, for example due to advanced age or deteriorating health.

2.3 In addition, the Deposit Insurance ("DI") scheme currently provides 100% coverage, subject to an aggregate cap of S\$20,000<sup>3</sup> per depositor per scheme member. The proposed increase in the level of coverage to 100% for PPF, which is also subject to aggregate caps, will align the approach of the PPF schemes with that of the DI scheme.

2.4 Furthermore, as explained in the second consultation paper, the introduction of the aggregate caps will similarly create an incentive for the policy owners to exercise prudence and market discipline in their selection of insurers. For those policies which are not subject to aggregate caps, the risk of moral hazard is limited as these policies are generally intended to indemnify losses as they occur.

## **3 Scope of Coverage of PPF Life Insurance Scheme**

### *Coverage of ILPs*

3.1 There were two enquiries on the coverage for Investment-Linked Policies ("ILPs") under the PPF life insurance scheme.

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<sup>3</sup> MAS has proposed to increase the cap to S\$50,000 in the consultation paper on "Review of the Deposit Insurance Scheme in Singapore" issued in February 2010.

### MAS' Response

3.2 As stated in the first consultation paper on PPF that was issued in December 2005, only the guaranteed benefits would be included in the coverage of the PPF life insurance scheme. In response to queries raised then, we have provided some examples to better illustrate what are the guaranteed benefits protected under the PPF life insurance scheme for ILPs in the response paper which was issued in August 2006. Please refer to Examples 3 to 5 in Appendix B of that response paper.

#### *Coverage of Annuities*

3.3 A few respondents asked if annuities would be covered under the PPF life insurance scheme, and if so, whether they would be subject to the aggregate caps of S\$500,000 for sum assured and S\$100,000 for surrender value. The respondents would like to know how the caps would apply to annuities during the deferment or payment stage, or when the annuity has no death or surrender benefit.

### MAS' Response

3.4 Only the guaranteed benefits under the annuity plan will be protected under the PPF life insurance scheme, and they will be subject to an aggregate cap. We recognise that it may not be easy to aggregate annuities with the other life insurance policies when applying the aggregate caps, given the product features of an annuity. Hence, we propose that the commuted value of the guaranteed benefits payable under the annuities (for death, surrender or annuity payments) be subject to a separate cap of S\$100,000. This is consistent with the cap on surrender value for non-annuity individual life policies.

#### *Coverage of Group Policies*

3.5 The second consultation proposed to exclude group insurance policies when aggregating the sum assured and surrender value to calculate the protection ratio to determine the PPF payout for the individual life insurance policies. It also mentioned that MAS is reviewing the proposal to subject group insurance policies to a separate cap. Though we have not received any response relating to the above

proposal, we propose the following caps on group life insurance policies that are involuntary<sup>4</sup>.

3.6 It is possible for the same life assured to be covered under different group schemes with the same insurer. However, it is generally not the insurer's practice to accumulate risk exposure/sum assured for involuntary group term schemes. The benefits are usually limited to a multiple (ranging from 24 to 36 times) of the monthly salary of the life assured, which further serves to mitigate the moral hazard risk. As such, we propose a cap of S\$100,000 per life assured per policy, instead of an aggregate cap per life assured for group term [e.g. Group Term Life offering coverage against death, total & permanent disability ("TPD") or critical illness] policies.

3.7 The proposed cap of S\$100,000 sum assured per life assured per group term policy is based roughly on the usual 24 times of the monthly salary, using average monthly earnings per employee of about S\$3,872<sup>5</sup>. We are not proposing any caps for Group Personal Accident and Health type of policies as these would not be subject to caps if sold by the general insurers. Lastly, although Group Endowment and Group Annuity policies are not commonly taken up, we propose, for completeness, the following caps to be consistent with the caps for individual life insurance policies (but applied on a per policy basis):

- (i) Group Endowment Policies: S\$100,000 for sum assured per life assured per policy (which is also consistent with group term policies) and S\$50,000 for guaranteed surrender value per policy; and
- (ii) Group Annuities: S\$100,000 for the commuted value of guaranteed benefits (for death, surrender or annuity payments) per policy.

#### *Coverage of Coupon Deposits, Advance Premium Payments and Unclaimed Monies*

3.8 The second consultation paper proposed that the PPF life insurance scheme will cover accumulated values of coupon deposits, advance

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<sup>4</sup> This refers to cases where the membership of the group scheme is compulsory. If the membership of the group scheme is voluntary, the relevant caps under the individual life insurance policies will apply.

<sup>5</sup> Source of information: MOM website that derived the figures based on the data from the CPF Board for 2009.

premium payments and unclaimed monies, without any aggregate caps imposed. No caps were proposed as the imposition of caps would introduce additional complications in levy computations without significant savings in the PPF costs. One of the respondents was of the view that the interest element of coupon deposits, advance premiums and unclaimed monies, which are usually not guaranteed, should not be covered to avoid moral hazard.

### MAS' Response

3.9 While the interest payable is not guaranteed for these amounts, the interest that has been accrued is a benefit guaranteed to the policyholders. As such, we propose to include the interest that has been accrued on proceeds left with the insurer under coupon deposits, advance premium payments and unclaimed monies, without any aggregate caps imposed.

### *Coverage of Personal Accident Policy*

3.10 In the second consultation paper, personal accident policies were not explicitly carved out as one of the type of policies to be excluded from the aggregate caps<sup>6</sup>. However, we have excluded personal accident type of riders (e.g. Accidental Death Benefit riders, Accidental Death and Dismemberment Benefit riders) from being included in the aggregate caps in the discussion on inclusion of term riders in the aggregation process.

### MAS' Response

3.11 Compared to a typical life insurance policy that provides protection against most causes of death, TPD or critical illness, a much higher sum assured can be purchased under a personal accident plan or rider for a much lower cost. This is because the payout is only limited to death or injury caused by an accident. The term of such personal accident policies can also be short. As such, if the sum assured under a personal accident policy is to be included in the aggregation for sum assured along with other relevant life insurance policies, the cap could be easily breached. This would offer little PPF coverage for the broader benefit offered by the other types of life insurance policies, which are of a longer term and guaranteed renewable nature. We therefore propose to explicitly exclude personal accident plans from the aggregate caps. This is consistent with

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<sup>6</sup> The policies excluded from the application of caps are long-term disability, long-term care and medical expenses policies.

the PPF general insurance scheme where no caps are imposed on the short-term personal accidental policies from a general insurer.

### *Coverage of Riders*

3.12 The second consultation paper proposed that all term riders be included in the aggregation process to calculate the protection ratio to determine PPF payout. One respondent asked if waiver of premium riders and accelerated benefit riders (e.g. riders that cover certain illnesses or disability, and accelerates the payment of part or all of the sum assured of the main policy when the claim happens) are covered under the PPF life insurance scheme. Another respondent commented that the sum assured of the accelerated benefit riders (e.g. accelerated Critical Illness term riders) should not be counted towards the aggregation of the caps.

3.13 Another respondent also enquired, for policies where the rider has a different life assured (e.g. payor benefit rider), how the aggregating of sum assured would be separated under the two different lives.

### MAS' Response

3.14 All types of riders, including those cited by respondents, would be covered under the PPF life insurance scheme. However, only term riders (e.g. level term, decreasing term, convertible term and critical illness term rider that provides for additional coverage instead of accelerating the benefits under the main policy) will be subject to aggregate caps, along with certain types of life insurance policies. It is not intended for payor benefit riders to be subject to aggregation.

3.15 We agree that in the case of term riders which accelerates the payment of part or all of the sum assured of the main policy, the sum assured of such riders should not contribute towards the aggregation of caps. We wish to clarify that the sum assured of accelerated term riders are not to be included in the aggregation process.

3.16 For clarity, Annex 2 sets out the types of policies or benefits which will be covered and aggregated for caps.

## **4 Scope of Coverage of PPF General Insurance Scheme**

4.1 One respondent wanted to clarify if the tuition fee protection business or bond business (for example, maid bond) would be covered under the PPF general insurance scheme.

## MAS' Response

4.2 Tuition fee protection business is not within the scope of the PPF general insurance scheme while the maid bond business is.

## **5 Application of Separate Protection Ratios to Sum Assured and Surrender Value**

5.1 The consultation paper proposed that separate protection ratios be applied to the aggregate sum assured and surrender value when calculating PPF payout. One respondent was of the view that a ratio that is applied to a policy in whole would be simpler and better. While having separate ratios for sum assured and surrender value would be simple at one point in time, it becomes unclear how a policy would behave subsequently. As each policy would have a relationship between sum assured and surrender value, the change in ratio for the two would make it unclear as to how the relationship between the sum assured and surrender value should proceed from that point until maturity.

## MAS' Response

5.2 Using a simple average protection ratio, whilst easy to execute for both levy calculation and working out the crystallised PPF payout and the liabilities to be transferred or run-off, would lead to anomalous results<sup>7</sup>. These results would be difficult to explain to the public, especially at the time when the claims are crystallised. We have thus proposed a more equitable way of applying the protection ratios separately to the sum assured and surrender value to avoid the situation of having the anomalous results.

5.3 We agree with the respondent that it is less straightforward to apply the different protection ratios for sum assured and surrender value when determining the amount of protected liabilities under a transfer or run-off scenario, as it would involve re-calculating the liabilities based on reduced benefits and revised premiums due to the aggregation.

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<sup>7</sup> To recap, these are scenarios which may occur after the application of the average protection ratio. For example, the aggregate sum assured of the policies may have to be scaled back even though the sum assured of the policies adds up to be less than the cap of S\$500,000, while the aggregate surrender value ends up being much greater than the cap of S\$100,000. Conversely, the aggregate surrender value of the policies may have to be scaled back even though the surrender value of the policies adds up to less than the cap of S\$100,000, while the aggregate sum assured ends up being much greater than the cap of S\$500,000.

5.4 However, we note that the need to re-calculate the protected liabilities based on reduced benefits and revised premiums as a result of the aggregation is only confined to cases where the caps are exceeded. Given that the aggregate caps of S\$500,000 sum assured and S\$100,000 surrender value fully cover about 98%<sup>8</sup> of all policy owners, we do not envisage that there would be voluminous cases requiring re-calculation. On the contrary, the anomalous results resulting from the simple average protection ratio method may lead to criticism that the PPF scheme is inequitable in its payout or that it short-changes claimants. Such reputational costs to the industry would most likely outweigh the costs of re-calculating the protected liabilities due to changes in benefits and premiums. We therefore maintain the proposal for the protection ratio to be applied separately to the aggregate sum assured and surrender value when calculating the PPF payout.

5.5 Nonetheless, we agree with the respondent that it is preferable to keep the method of determining the protected liabilities for the purpose of levy calculation simple, and one which follows closely to the current valuation of liabilities done by the insurers. Given that levies are only proxies of the exposure of PPF, it may be administratively cumbersome for the insurers to re-calculate the protected liabilities, as they will have to take into account the different extent of changes in benefits and reductions in premiums. Furthermore, such calculations are limited to cases where the caps are exceeded. On average, we would expect that applying a simple average ratio uniformly to the guaranteed policy liabilities should give us a reasonable proxy of the exposure of PPF. There is also no need to explain the anomalous results to the policy owners given that the computation is for levies and not for the payout. We therefore propose to use the simple average protection ratio for the purpose of calculating the PPF levies.

## **6 Role of SDIC**

### *Administration of PPF Schemes*

6.1 A respondent suggested that to reduce the cost of administration, the SDIC should call for a tender from the industry on administering liabilities which are to be run-off.

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<sup>8</sup> This threshold was communicated in the first consultation paper in December 2005, and still holds true.



### MAS' Response

6.2 In the event that the run-off approach is adopted, SDIC will set up a company to hold the policies although administration of the policies will be outsourced to a third party, which is likely to be an insurer.

### *Consumer Education*

6.3 Another respondent asked if the role of SDIC, in relation to consumer education, would be confined to the PPF schemes.

### MAS' Response

6.4 SDIC's role in consumer education pertains to educating the public on the PPF schemes and not on insurance awareness.

## **7 Conditions for Using PPF Funds**

7.1 One respondent asked if MAS or SDIC would issue a public report on their findings and the rationale for triggering payouts whenever such payouts are made, in order to improve the transparency of the payout process.

### MAS' Response

7.2 In the event of a PPF payout, MAS will explain the basis of its decision for triggering the payout. However, MAS may not be at liberty to disclose further details in view of the sensitivity of certain information.

## **8 Investment of PPF Funds**

8.1 The second consultation paper proposed that PPF funds should be invested in any security issued by the Singapore Government, Singapore dollar deposits with MAS and such other investments as may be approved by the Minister. One respondent was of the view that the investment mandate for PPF funds was restrictive and suggested that it be widened slightly, so as to reduce costs to insurers. Another respondent proposed that for transparency, "such other investments as may be approved by the Minister" be restricted to a published list of investments. The same respondent was concerned that if any such investment resulted in a material loss to the PPF schemes, insurers would be required to bear the loss.

## MAS' Response

8.2 PPF funds should only be invested in safe and liquid assets so that payouts could be made expeditiously to policy owners in the event of a PPF trigger. As such, PPF funds should only be invested in assets that meet the objectives of capital preservation and maintenance of liquidity. Given that financial markets evolve quickly, and new types of assets that meet such objectives may emerge in future, it would not be practical to confine the permissible investments to a pre-determined list of investments. However, as a safeguard, investment of the PPF funds in assets other than those prescribed in the Act would have to be approved by the Minister, after satisfying that the objectives of capital preservation and maintenance of liquidity.

## **9 Liquidity Provision**

9.1 The second consultation paper proposed that in the event that payouts exceed the size of the PPF funds, SDIC would be empowered to borrow to finance the shortfall. One respondent asked if insurers would be required to fund the interest on the borrowing, or whether special credit facilities would be extended to the SDIC to keep the cost of the interest to a minimum.

## MAS' Response

9.2 When sourcing for credit facilities to finance any shortfall, the cost of any such borrowing will be a factor taken into consideration to minimise the financial impact to the PPF. If the other insurers are able and willing to fund any shortfall immediately, this option will be explored further at that point in time, as it would reduce the amount of financing costs.

## **10 Levy Assessment**

### *Risk-Based Levies*

10.1 The first consultation paper proposed imposing risk-based levies, based on the CRAFT<sup>9</sup> supervisory rating, on the insurers. One

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<sup>9</sup> CRAFT stands for Common Risk Assessment Framework and Techniques. CRAFT was developed by MAS to assess the risks of a financial institution and its internal controls and risk management.

respondent suggested that the PPF levies be based on the Capital Adequacy Ratio (“CAR”) of insurers, instead of being just a component of the risk ratings, as the CAR is an objective measure of the financial soundness of an insurer.

10.2 Another respondent suggested that a more equitable manner would be to base the levy on the aggregate risk requirement rather than on the liabilities, adjusted for the CAR of the insurer, with a higher CAR leading to a lower levy rate. The respondent felt that two insurers with the same value of protected liabilities may have very different risk profiles and policy liabilities alone do not reflect other risks (especially asset and asset-liability risks) that an insurer may undertake. In addition, it would be more equitable to apply a 25% levy rate to the base value at the end of each quarter, rather than to apply 100% of the rate to the base value at the end of the preceding year, in order to reflect the changing risk profile of the insurer through the year. Another respondent was of the view that since all insurers are required to meet solvency requirements, it would be more equitable to have one percentage rate applicable to all insurers, rather than impose levies based on the risk ratings of insurers.

#### MAS’ Response

10.3 The CAR and risk requirements are components of the Risk-Based Capital (“RBC”) framework that aims to put in place a more transparent and risk-focused capital and valuation framework that reflects all major financial risks of insurers. However, the CRAFT rating, which the PPF levies would be based on, encompasses more than just the financial risks of insurers. It takes into account other factors (for example, other non-financial risks, risk management and controls, and parental support) and is more reflective of the overall risk rating, as well as risk of default, of the insurer. The introduction of risk-based levies would also provide an incentive for insurers to manage their risks better. Under normal circumstances, we would not expect an insurer’s overall risk rating to fluctuate drastically from year to year. In general, it would not be administratively efficient or justifiable (given the relatively low levy contributions) to have more a frequent, such as quarterly, assessment of the levies.

#### *Differentiation in Levy Rates*

10.4 The following risk-based levy structure was proposed in the first consultation paper:

<b>Supervisory Ratings<sup>10</sup></b>	<b>Life insurance PPF</b>	<b>General Insurance PPF</b>
Low	0.017%	0.13%
Medium Low	0.020%	0.15%
Medium High	0.035%	0.27%
High	0.150%	1.15%

10.5 One respondent commented that the risk-based levy structure was highly differentiated between the “Low” and “High” risk rating categories. As the overall risk rating is a subjective assessment and can be changed from year to year, the respondent felt that a highly differentiated levy between insurers was inequitable. Instead, a lower differentiation would be better, as the pre-funding approach is meant to be built up over a period of time. Insurers would have ample time to manage the levy payment and hence their risk rating over time. The respondent proposed that the differentiation should be phased in slowly, with no differentiation at the beginning before moving to a bigger differentiation (albeit not as big as the original proposed in the first consultation paper) over time.

#### MAS’ Response

10.6 The levy rate for each risk rating category reflects the relative differences in the risk contribution to the PPF schemes by scheme members in the different categories. For example, the risk of loss to the PPF scheme arising from the failure of a scheme member in the “Low” risk rating category is significantly lower than the risk posed by a scheme member in the “High” risk category. Nonetheless, MAS will review the differentiation between the levy rates among the different risk rating categories when we rework the target fund sizes of the PPF schemes closer to the date of the PPF implementation. We will also review if there is a need to extend the build-up period to make levies more affordable to the scheme members.

#### *Submission of Information for Levy Assessment*

10.7 Currently, year-end statutory reporting, stress testing exercises and participating fund bonus reviews take place in the first quarter of each year. One respondent asked if the date for submission of information for the purpose of levy assessment could be revised to 30 June, rather than 30 April as proposed in the consultation paper.

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<sup>10</sup> A low supervisory rating indicates lower risk.

## MAS' Response

10.8 We do not propose the use of overly complicated calculation methods for the purpose of levy assessment. As such, it is not envisaged that the information to be submitted by the insurers for the purposes of levy assessment would be substantially more onerous than what insurers have to submit for the year-end statutory reporting.

10.9 Details of the information to be collected will be finalised at a later date, but we expect that the information required will include:

### For life business:

- (i) Amount of protected liabilities<sup>11</sup> for the different funds maintained separately, in a format similar to Form 14<sup>12</sup> in the Insurance (Accounts & Statements) Regulations, on an annual basis; and
- (ii) Accumulated value (i.e. inclusive of interest which has been accrued as at valuation date) of the coupon deposits, advance premium payment and unclaimed monies.

### For general business:

- (i) Breakdown of the gross written premium and policy liabilities by the protected classes of business;
- (ii) Number of policies under PPF-covered lines of general insurance business; and
- (iii) Number of claims incurred for the past year for PPF-covered lines of general insurance business.

10.10 The information which insurers are required to submit for the purpose of levy assessment is largely similar, albeit more granular, to what insurers have to prepare for the year-end statutory reporting. To allow insurers sufficient time to collate the information, we have already allowed for an additional month from the due date of the annual statutory submission (i.e. 31 March). The deadline of 30 April has been set taking

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<sup>11</sup> The calculation of protected liabilities would only take into account the guaranteed benefits, and the relevant caps. A simple average protection ratio method as set out in the first consultation paper is allowed solely for the purposes of levy assessment (and not at the PPF payout stage).

<sup>12</sup> Form 14 is an abstract of valuation results of life business.

into account the need to process the information submitted before collecting the levies in July.

#### *Levy Assessment for New Insurers*

10.11 One respondent noted that for a new insurer, the levy would be nil for the first year of operation as it would not have any protected liabilities on 31 December of the preceding year, in the case of a life insurer, or gross written premium received or receivable for protection classes of business from 1 January to 31 December of the preceding year, in the case of a general insurer. The same respondent suggested that the levy be computed on a quarterly basis instead, which would then require the new insurer to start paying a levy during that year.

#### MAS' Response

10.12 For ease of administration<sup>13</sup> and on account of the relatively low levy contributions, it would not be practical to have more frequent, such as quarterly, assessment of the levies, as suggested by the respondent. In the case of newly licensed insurers for which there is no data for levy assessment, we propose that they be charged the pro rata minimum premium as a nominal contribution for the benefits conferred by membership in the PPF scheme. This is consistent with the approach taken for the DI scheme. The minimum premium (which is proposed at S\$2,500) will be pro-rated according to the number of months remaining for the year and will be payable 1 month from the commencement of operation.

#### *Treatment of New Entrants*

10.13 The consultation paper noted that levies may be reduced or stopped when the target fund size is reached. One respondent was of the view that this should not apply to new insurers registered subsequent to the fund size reaching its target, unless a fair basis of calculation can be devised to determine the amount of levies to be imposed on the new insurer.

#### MAS' Response

10.14 We intend to provide in the new PPF regulations that MAS and SDIC may conduct a joint review of the premiums when the target fund

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<sup>13</sup> Premiums for DI are assessed only once a year for premium contributions by SDIC.

size has been reached or exceeded. This is currently provided for in the DI regulations<sup>14</sup>.

10.15 We agree that there should be an equitable method of computing the contributions of new insurers admitted after the build-up of the fund to its targeted size, and would take parity into consideration in our subsequent review. One possible approach could be to continue to levy new entrants, even after the target fund size has been reached or exceeded, on the same levy scale and over the same build-up period as the insurers who had become members at the inception of the fund. However, as the funding for the PPF schemes have not commenced, it is not critical at this juncture to decide on the approach to take for new entrants when the target fund size is reached. We will consult the industry again when the review is completed.

## **11 Priority Ranking of Unsecured Liabilities**

11.1 Two respondents were of the view that to increase the protection of policy owners' rights and to reduce the levy required, preferential debts should rank below those of direct policy liabilities.

### MAS' Response

11.2 For clarification, preferential debts are defined under Section 328(1) of the Companies Act. These include items such as:

- (i) All costs, charges and expense incurred in the winding up, including the remuneration of the liquidator;
- (ii) All wages or salaries, and amounts due to an employee as a retrenchment benefit or ex-gratia payment<sup>15</sup>;
- (iii) All amounts due in respect of contributions payable by the employer for the employees' superannuation or provident funds;
- (iv) All remuneration payable to any employee in respect of vacation leave;

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<sup>14</sup> Regulation 10(2), Deposit Insurance Regulations 2006

<sup>15</sup> Subject to a cap that is equivalent to 5 months salary or \$7,500, whichever is the lesser.

(v) All amounts due in respect of work injury compensation under the Work Injury Compensation Act; and

(vi) All tax assessed and all goods and services tax due.

11.3 The above items are legitimate expenses that should be deducted from the insurance funds before policy owners' liabilities are paid. It is also common in a number of jurisdictions<sup>16</sup> for preferential debts to rank above policy owners.

## **12 Others**

### *Pre-Funding Approach*

12.1 One respondent opined that a pre-funded scheme would tend to be costly to administer and maintain, particularly if done via a separate body. A review should be conducted before deciding whether to adopt a pre-funded approach for the PPF schemes.

### MAS' Response

12.2 The proposal for a pre-funded approach for the PPF schemes was included in the first consultation paper on PPF. Adopting such an approach for the PPF schemes is the most equitable as the failed insurer would have contributed to the fund prior to failure. Having pre-funded PPF schemes would also enhance the credibility of the scheme, as well as expedite payouts in the event of default by an insurance company. As such, we will maintain the original proposal to introduce pre-funding for the PPF schemes.

### *Target Fund Size*

12.3 Two respondents enquired how the target fund sizes for the PPF schemes were derived. While the size of the levy does not seem unreasonable, they were of the view that greater transparency on the derivation of the levy rate would be in the interests of all insurers, as they would know if the rate is adequate. This is particularly relevant as any unfunded costs of any failing insurers would be picked up by the remaining insurers. One of the respondents noted that the target fund size for the PPF general insurance scheme is 1.5% of protected liabilities.

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<sup>16</sup> New York, UK, Australia, etc.



This is relatively significant compared to the PPF life insurance scheme, which is 0.2% of protected liabilities.

### MAS' Response

12.4 The models used for deriving the PPF life insurance and general insurance funds were largely adapted from the model used for the DI fund. 100,000 Monte Carlo simulations were run and the 100<sup>th</sup> highest loss was taken as the optimum fund size (i.e. 99.9% confidence level). MAS will rework the levies closer to the date of the PPF implementation, especially given that the target fund sizes obtained previously were based on 90% PPF coverage for the life insurance policies and the non-compulsory general insurance policies protected under the PPF general insurance scheme.

### *Charging of Levies to Insurance Fund*

12.5 Some respondents sought clarification as to whether each insurance fund would bear the costs of its own PPF levy. To avoid cross subsidies between insurance funds, one of the respondents emphasised the need to have separate levies for different insurance funds (e.g. participating and non-participating funds) within the PPF life insurance scheme. This would ensure that participating fund policy owners, who bear 90% or more of the risks of the fund, do not subsidise non-participating fund policy owners who bear 0% of the risks of the fund.

### MAS' Response

12.6 The levy rate (which ranges between 0.017% and 0.15%) is not distinct between the different insurance funds within the PPF life insurance scheme as we are not implying that any insurance fund is at a higher risk of causing the insurer to fail. The CRAFT rating is also not issued specifically to any insurance fund. To prevent cross-subsidisation however, each insurance fund would only bear the costs of its own share of the PPF levy. But this is subject to limits, which is calculated as the simple average of the annual risk based levies for the “Medium Low” and the “Medium High” supervisory rating categories<sup>17</sup>, to ensure that policy owners are not penalised for the weaknesses in their insurer’s internal controls by having to bear higher levies.

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<sup>17</sup> This is as proposed in the response paper issued in August 2006 in response to the first consultation paper for PPF.

12.7 For example, a life insurer has two life insurance funds – participating fund and non-participating fund. The protected liabilities in the participating fund were S\$100m at the levy assessment date, whilst the protected liabilities in the non-participating fund were S\$500m at the levy assessment date. Assuming that the risk rating of the life insurer was “Medium High”, the participating fund would only be allowed to bear S\$27,500 (0.0275%, i.e.  $(0.02\%+0.035\%)/2$  of S\$100m) of the PPF levies, whilst the non-participating fund would bear S\$137,500 (0.0275% of S\$500m) of the PPF levies.

#### *Implementation Date*

12.8 Two respondents enquired about the implementation date for the revised PPF schemes. One of them asked for sufficient notice to be given so that insurers could budget for the PPF levy contributions in their business plans.

#### MAS' Response

12.9 We target to implement the revised PPF schemes in 2011, after the necessary legislation changes have been made. Members will be given sufficient lead time before the revised PPF schemes become operationalised.

MONETARY AUTHORITY OF SINGAPORE  
17 AUGUST 2010

**RESPONDENTS TO THE SECOND CONSULTATION ON PPF**

- (1) Life Insurance Association<sup>18</sup>
- (2) Lockton Companies (Singapore) Pte Ltd
- (3) MSIG Insurance (Singapore) Pte Ltd
- (4) QBE Insurance (International) Limited
- (5) Mr Walter Leong

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<sup>18</sup> The Life Insurance Association submitted comments on behalf of 8 insurers, namely, Aviva, Great Eastern, HSBC Insurance, Manulife, Prudential, Swiss Life, Transamerica and UOB Life.

## Annex 2

This is not meant to be an exhaustive list. It is meant to illustrate what will be covered under the PPF life insurance scheme and what is subject to caps.

	Type of individual life insurance policy/benefits	Covered under PPF?	Aggregate Caps, applicable per life assured per insurer		
			Sum Assured \$500,000	Surrender Value \$100,000	Annuities \$100,000
1	Investment-linked policy (including portfolio bond)	Yes, guaranteed benefits only	✓	✓	
2	Single or regular premium endowment policy	Yes, guaranteed benefits only	✓	✓	
3	Single or regular premium anticipated endowment policy (i.e. with regular coupon payments)	Yes, guaranteed benefits only (Including coupon deposits left with the insurer)	✓	✓	
4	Single or regular premium whole of life policy	Yes, guaranteed benefits only	✓	✓	
5	Annuity (deferred or immediate)	Yes, guaranteed benefits only			✓
6	Term policy (including mortgage decreasing term or level term policy)	Yes	✓		
7	Personal policy or rider	Yes	No caps applicable		
8	Medical Expenses Plan	Yes	No caps applicable		
9	Long-term Care (e.g. Eldershield)	Yes	No caps applicable		
10	Disability Income	Yes	No caps applicable		
11	Term riders (e.g. convertible term, renewable term, additional critical illness)	Yes	✓		
12	Other riders (e.g. waiver of premium, payor benefit, family income benefit)	Yes	No caps applicable		
	Type of compulsory group life insurance policy/benefits	Covered under PPF?	Caps, applicable per life assured per policy per insurer		
			Sum Assured \$100,000	Surrender Value \$50,000	Annuities \$100,000
13	Group Term (e.g. Group Term Life, Group TPD, Group Critical Illness)	Yes	✓		
14	Group Endowment	Yes, guaranteed benefits only	✓	✓	
15	Group Annuity	Yes, guaranteed benefits only			✓
16	Group Health	Yes	No caps applicable		
17	Group Personal Accident	Yes	No caps applicable		