

December 8, 2010

Dear insurers,

Re: Catastrophe Risk Return Guidelines (“Cat guidelines”) and Catastrophe Risk Return (“Cat Return”) template

The Bermuda Monetary Authority (“the Authority”) wishes to thank the stakeholders for their continued support of our key initiatives. Recently, the Authority published Cat Return and Cat guidelines and a number of comments were received. The Authority is committed to engaging our stakeholders in such initiatives as we strive to achieve our supervisory objectives, while retaining Bermuda’s role as a key player in international fora.

The Authority’s responses to the comments that were received are outlined below.

a) Cat Return template

Concerns were raised on various aspects of the Cat Return template.

The Authority does acknowledge the concerns raised on the Cat Return. The Authority is committed to working with the market in revamping its regulation while at the same time minimising costs to insurers. Accordingly, the Authority has made changes to the proposed Cat Return to take into account the market’s suggestions. The Authority envisions the Cat Return as a complement to the BSCR filing and actually replacing a filing with which many insurers are currently experiencing problems. The Cat Return seeks to understand catastrophe exposure at the level of detail that facilitates the Authority’s understanding of the gross and net probable maximum losses (PMLs) currently submitted by insurers in Schedule V in accordance with the Insurance Prudential Standards (Class 4 Solvency Requirement) Order 2008 (the ‘Order’). This information is critical given that the PMLs are a major contributor to the Enhanced Capital Requirement (“ECR”). The Cat Return will allow a greater degree of comparison between different modelling implementations than is currently the case. The Authority considers these benefits as important components in revamping its regulatory regime.

b) Cat Return page 3 to 11: Exceedance Probability (EP) curves & paragraph 18 of Cat guidelines

Comments were raised on the content and format of the EP curves.

The Authority has significantly revised the information to be reported on EP curves. This includes eliminating the EP curve for reinsurance. Further, the EP curve for insurance will not be required, except where the percentage of net insurance premiums written is greater than 10% of total net premiums written. EP curve sheets on regions-perils have also been revised to require insurers to submit only quantitative information on EP curves. Qualitative information on EP curves will only be required for the ‘EP curve total’ and the ‘EP curve insurance’.

c) Cat Return Page 3 to 11 EP curves: insurance policies without limits

Clarity was requested on how to account for policies in Europe and Asia that do not have limits.

The Authority does recognise that certain insurance policies in Europe and Asia do not have limits or Total Insured Value (“TIV”). Accordingly, the Authority has revised the Cat Return to allow insurers to report on such policies with non-determinable TIV or with no limits. That being the case the Authority does acknowledge that ratios involving aggregate TIV have limitations in this context and that comparison of Europe/Japan ratios with for example, US hurricane ratios would be misleading. The Authority will work with insurers, in circumstances where the information requested in the Cat Return does not capture the specifics of its business.

d) Page 3 to 11: EP curves: the average loading factor to ground up losses estimates

Concerns were raised on the request to submit average loading factor to ground up losses for each region-peril given the complexity of re-running the models.

The Authority does recognise that the average loading factor calculation could be potentially difficult for some insurers. Accordingly, the Authority has revised the EP curve sheets to request the average loading factor for only the ‘EP curve total’ and the ‘EP curve insurance’. The Authority considers the loading factor to be important given the non-linear nature of loss to excess layers (see Appendix A of the guidance notes to the Cat Return).

e) Page 2 of 19 Zones 11 and 12 and lines of business

Clarification was requested on the definition of lines of business.

The Cat Return includes a glossary defining the zones and lines of business. We have also included input messages within each cell describing these requirements. Further, zones and lines of business have been defined in Schedule III and V respectively of the Order.

f) Page 19 of 19: Assumed exchange rates

Clarity was requested on details surrounding assumed exchange rates.

The Authority has amended the Cat Return to require insurers to include the exchange rate(s) used to translate amounts to US dollars for the ‘EP curve total perils’ only.

g) Cat Return trial run filing

Comments were requested on the Cat Return trial run filing dates.

The Cat Return trial run template will be embedded in the 2010 filing documents. However, the Authority proposes to extend the deadline to June 2011. Insurers wishing to avail themselves of this extension will be supplied with standalone documents. The Authority will not require submission of the catastrophe information at year-end which the Cat Return is intended to replace (this is exposure limits and probable maximum loss, both gross and net, by statutory line of business, by insurance and reinsurance, and by statutory territory).

h) Paragraph 8: comparability of Cat Return data

Concerns were raised on the data quality and hence comparability of that data across insurers.

The Authority does acknowledge that the data comparison across insurers will not be a perfect comparison, given the unique characteristics of individual insurers. While general comparison of metrics within the Cat Return may be elusive, it allows the Authority to understand the catastrophe exposure and methodologies employed. However, the Authority envisions that by isolating the various components/choices of cat model /‘dials’/modelling options, etc. that are included in the modelling process, there will certainly be some harmonisation of data to identify similarities and outliers. The identified outliers do not necessarily raise a concern, but rather provide an opportunity for the Authority to understand the unique characteristics of the insurer. The Cat Return forms one component of the Authority’s supervisory process, therefore it shall not be reviewed in isolation but rather analysed alongside other information received (from other returns). Where the Authority requires further information /clarification, it will hold discussions with the respective insurer.

i) Paragraph 15: publishing of Cat Return data

Clarity was requested on the particulars of the Cat Return data to be published.

While the specific details of the information to be published are still being developed, it is envisioned that aggregated information would be published. This we believe will not result in confidentiality issues.

j) Paragraph 26 -28: EP curve information

Clarity was requested on the following:

- ***Should offshore and marine losses be included for all region-perils?***
- ***Should the intra-group reinsurance be modelled for recoveries?***
- ***Does ‘business segments’ mean the same as region-perils?***

Offshore and marine losses should be included for all region-perils. Generally the principle to be observed is that anything that might cause correlated losses from an event should be included for all region-perils. Further, the Authority requires that intra-group net losses be modelled for recoveries. 'Business segments' refers to the aggregated business written in region-perils.

k) Paragraph 28 (page 13): limits exposed calculation

Clarity was requested on whether the limits exposed are calculated at group level.

Limits exposed should be calculated as the sum of all limits providing contractual protection for the insurance, reinsurance, and combined insurance and reinsurance-basis respectively under consideration. Where business is not subject to an aggregate or occurrence limit, the insurer should include premium in the cells provided on a gross and net basis ('Total gross premium without an occurrence or aggregate limit' and 'Total net premium without an occurrence or aggregate limit'). Where total insured values are not determinable (for lines of business such as workers' compensation for example) insurers should include the premium in the cells provided on a gross and net basis ('Total gross premium with non-determinable TIV', 'Total net premium with non-determinable TIV').

l) Paragraph 61-71: terrorism exposure

Clarification was requested on:

- ***Whether the required terrorism exposure relates to US or worldwide.***
- ***Details on target location.***

The Authority is requesting terrorism exposure on a worldwide basis. However, the Authority does recognise limitations of certain catastrophe models. The Authority believes that insurers writing significant terrorism exposure outside of the United States should be aware of their exposure. The Authority has included guidelines on target location.

m) Paragraph 68-71: terrorism reinsurance limits

Concerns were expressed on the granularity of information requested on terrorism reinsurance limits.

The Authority does recognise that information capture and transfer can lead to less transparency at the level of the reinsurer. The Authority is also aware that reinsurers offer terrorism coverage on some of these exposures that have a high potential of losses occurring. Where the determination of aggregate exposure from terrorism to a reinsurance contract cannot be determined, but terrorism coverage is provided, the Authority requires reinsurers to include 100% of the terrorism limit provided.

The Authority again thanks stakeholders for their comments on the Cat Return and Cat Guidelines. We are committed to working with the Industry and other stakeholders to ensure a result that is in the best interest of the Bermuda market, taking into account the costs to the Industry.

Please feel free to contact the Authority if you have any questions.

Yours sincerely,

Bermuda Monetary Authority