



To: Class 4 Insurers

From: Oronde Walker

Date: 15 August 2008

Subject: Amendments to the Bermuda Monetary Authority's Insurance Statement of Principles

Please find attached to this memo, proposed amendments which will be included in the Bermuda Monetary Authority's ("the Authority") Statement of Principles ("SOP"). The amendments to the current SOP outline the Authority's proposed application of the *Insurance Act 1978* ("the Act") with respect to the administrative procedures associated with the Capital Add-on Policy ("the Policy") pursuant to the *Section 6D* of the Act. Please note that the Policy was presented to industry for consultation from June 18, 2008 until July 18, 2008.

In connection with the introduction of the Policy, the Authority seeks views to the amended SOP before finalizing and publishing. The views of the insurance industry and of other interested persons should be sent to policy@bma.bm no later than September 15, 2008.

Please note that the Authority thanks you in advance for your responses as it is critical to have your input as we continue to enhance our risk-based regulatory regime.

If you have any further questions or concerns regarding this issue, please feel to contact me.

Sincerely,

Oronde Walker
Principal (Policy)

Insurance Act 1978

Section 2A: Statement of Principles

The Insurance Statement of Principles Act will be amended by adding Part 7 which will follow Part 6 and include the following:

PART 7 Capital Add-On Policy

1. The Authority only proposes to apply the capital add-on under exceptional conditions. These circumstances relate to a significant deviation between the insurer's risk profile and (1) the underlying assumptions of the Bermuda Risk-Based Capital model ("BSCR") or an approved internal model pursuant to the *Section 6D* of the Act and/or (2) the insurer's self-assessment of its risk management policies and practices. With respect to the latter, the Authority proposes to allow insurers to determine the operational risk charge component of the Enhanced Capital Requirement ("ECR") via a self-assessment of its risk management program pursuant to the *Section 6D* of the Act.
2. Exceptional circumstances may arise from the following areas:
 - a. operational risk charge;
 - b. provisions for reserve deficiencies or premium inadequacies;
 - c. significant growth in premiums;
 - d. notification under Section 8A(f) of the Act; and
 - e. report made under Section 31AA(1)(b) of the Act.
3. Circumstances where capital add-ons may be applied include:
 - a. **Operational risk charge:** Where the Authority believes that the operational charge self-assessment, subsequent to an onsite inspection, does not reasonably reflect the insurer's risk management policies and practices, an add-on may be applied to the operational risk charge.
 - b. **The ECR is affected by the insurer's reserving levels:** Where the Authority believes that either the insurer has under reserved or unearned premiums are insufficient to cover the insurer's future liabilities, a capital add-on may be assessed.
 - c. **Significant growth in premiums:** Where the Authority believes that projected business activity, in the insurer's case, will vary materially from the actual prior year's activity then a capital add-on may be assessed.
 - d. **Sections 8A(f) and 31AA(1)(b) of the Act:** Where the Authority believes that a significant events has a material impact upon the insurer's reserving levels and ability to collect from creditors, a capital add-on may be assessed.

4. Circumstances where a capital reduction may be applied include:
- a. **Non-admitted assets:** Where the Authority gives the insurer credit for hybrid capital on application by the insurer, a capital reduction may be assessed.
5. The Authority supports due process and proposes to introduce an appeals process for an insurer aggrieved by the Authority's decision to apply a capital add-on. In this regard, the Authority proposes the following administrative process surrounding capital add-ons:

-  The Authority will notify the insurer of its intention to adjust its available statutory capital and surplus or ECR and provide the insurer with the opportunity to make representation. All adjustments are prospective from the date of the assessment and do not impact the prior year's statutory filings.
-  The insurer will have 28 days to make representation to an in-house panel at the Authority comprising of Risk, Actuary, and Supervisory staff members at the Authority.

Should the insurer decide to forgo an appeal, the adjustment or charge will come into effect not less than 90 days after notification.
-  If the insurer appeals, the in-house panel will consider the representation of the insurer before reaching a decision. Once a decision is reached by the in-house panel, the insurer will be notified of the Authority's final decision. The adjustment will be effective 90 days or longer from the date of the final decision as determined by the Authority.
-  Where the insurer does not accept the in-house panel decision, the insurer may appeal to a tribunal pursuant to Section 44A Part VIIIA of the Act. The adjustment will be effective 90 days or longer from the date of the Tribunal's decision as determined by the Authority.

The capital add-on process is outlined in the following schematic:

