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BMA Consultation Paper: Proposed Enhancements to the Regulatory Regime for Commercial Insurers (CP2)

Connecting the Dots | CP2 Governance and Risk Management Series | Part 1

Part 1 of Deloitte's Connecting the Dots | CP2 Governance and Risk Management Series will summarize the key updates to the regulatory regime as outlined in the following sections of the BMA's consultation paper, Proposed Enhancements to the Regulatory Regime for Commercial Insurers:

Section 2.2
New Formal SBA Application Process

Section 2.3
Liquidity Risk Management

Section 2.7
Changes to Default and Downgrade Cost Assumptions

Section 2.8
Liquidity and Transaction Cost

Section 2.2 – New Formal SBA Application Process

Whilst the SBA (Scenario Based Approach) has been used by Companies, even prior to the CP1 and CP2 announcements, the BMA has now tightened regulations by formalizing the application process. **Effective March 31, 2024**, companies might find themselves in one of 4 positions:

Company Position	Approval Required?
Newly licensed insurers that propose to use the SBA	✓
Existing Insurers currently not using the SBA who want to switch over to the SBA	✓
Existing Insurers that already use the SBA	✗
Existing Insurers that already use the SBA that have material changes (The SBA model change policy Section 2.14, should define major and minor model changes)	✓
Existing Insurers that already use the SBA that is writing a new Line of business	✓

Timeline: 4 – 8 weeks / 8+ weeks

The BMA encourages that applicants engage in pre-application discussions. If done, the application process will take between 4 – 8 weeks. If not, the process might require additional review time.

Alert: The updated regulations disallow the splitting of insurance contracts purely to achieve SBA eligibility.

The application package should include (but is not limited to):

- Evidence that the criteria for using the SBA model is met
- The completed **SBA reporting template**
- The **Full SBA** model calculations
- **Stress tests** (see Section 2.4 for more guidance)
  - 2 stresses to be prescribed by the BMA
  - Insurer-specific liquidity stress tests
  - Liquidity risk management and liquidity plans (Section 2.2)
  - Lapse stress tests
- Documentation relating to:
  - **Key assumptions & data used**
  - Detailed explanations of the **calculation process**
  - **Methodologies**
  - **Governance structure** (Including validation framework)
  - **Model change policy**
  - **Validation report** by an external party and/or independent validation function
- The model risk management in place
- Overview (graphically) and description of the **systems, infrastructure, and people** relevant to the SBA model.
- **External dependencies** (such as vendors or consultants)
- All other documents listed in the SBA reporting template, and any additional info the insurer thinks might be necessary for the assessment and decision by the BMA.

Section 2.3 – Liquidity Risk Management

Whilst there is a lot of focus on the SBA model and the governance around it, the liquidity risk management requirements have been extended to not only apply to companies that use the SBA but also to companies that **do not,** but who are exposed to mass lapse risk. **The BMA has introduced requirements for insurers to implement a liquidity risk management program, that covers at a minimum:**

Governance and Risk Appetite

The board of directors is responsible for ensuring that the Insurer has an effective **liquidity risk management framework**, including clear ownership in the organization of key elements of the framework. This framework should be **reviewed annually** (at a minimum) and clearly define the roles and responsibilities of the **first and second Lines of defense.**

The insurer should have a thorough understanding of the company's sources of demand and supply of cash, and the level of liquidity risk the Insurer has an appetite to seek or accept should be formalized through **a board approved liquidity risk appetite**.

The liquidity risk appetite should be **documented** (either as a stand-alone document or as part of the company's governance documents).

Cash Needs and Source Register

The insurer should maintain a cash needs and sources register which keeps record of each cash need and the potential sources of liquidity.

Liquidity Buffer

The insurer should have a pool of highly liquid assets set aside that can be used to address any deficiencies in cashflow that might arise.

Stress and Scenario testing

A balance should be struck between severity and plausibility.

Liquidity Contingency Plan

A liquidity contingency plan should be documented to serve as a playbook incase of a liquidity deficit. **Clear triggers** should be identified and reviewed regularly. In addition, the plan should **be tested regularly through dry-run simulation** exercises.

Monitoring and Reporting

The insurer should put in place appropriate infrastructure and systems to access relevant data and, thus access and monitor its liquidity exposures.

Section 2.7 - Changes to Default and Downgrade Cost Assumptions

Key Control

The Chief Actuary and Chief Investment officer needs to attest on the prudence and appropriateness of the default assumptions submitted for approval to the Authority, including confirming compliance with regulatory requirements.

Section 2.8 - Guidance on Liquidity and Transaction Costs

Alert: Like all other assumptions in the SBA, the liquidity and transaction costs should be subject to internal challenge within the Insurer, independent assessment by the approved actuary and reported to the BMA as part of the enhanced SBA reporting.

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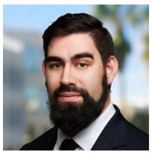

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