

**41<sup>ST</sup> MEETING OF THE INSURANCE COUNCIL OF SAINT LUCIA,  
SANDALS LA TOC HOTEL, OCTOBER 4, 2016**

Remarks by  
Insurance Manager, Financial Services Regulatory Authority

President of the Insurance Council, Distinguished  
Guests, members of the Insurance Council, ladies and  
gentlemen good afternoon

On behalf of the Board of Directors and the  
Management and Staff of the FSRA, I thank the  
Insurance Council for this invitation to address you at  
your 41<sup>st</sup> Annual General Meeting.

My address today will focus mainly on three areas:

- The performance of the insurance industry;
- Pricing; and
- Reserving

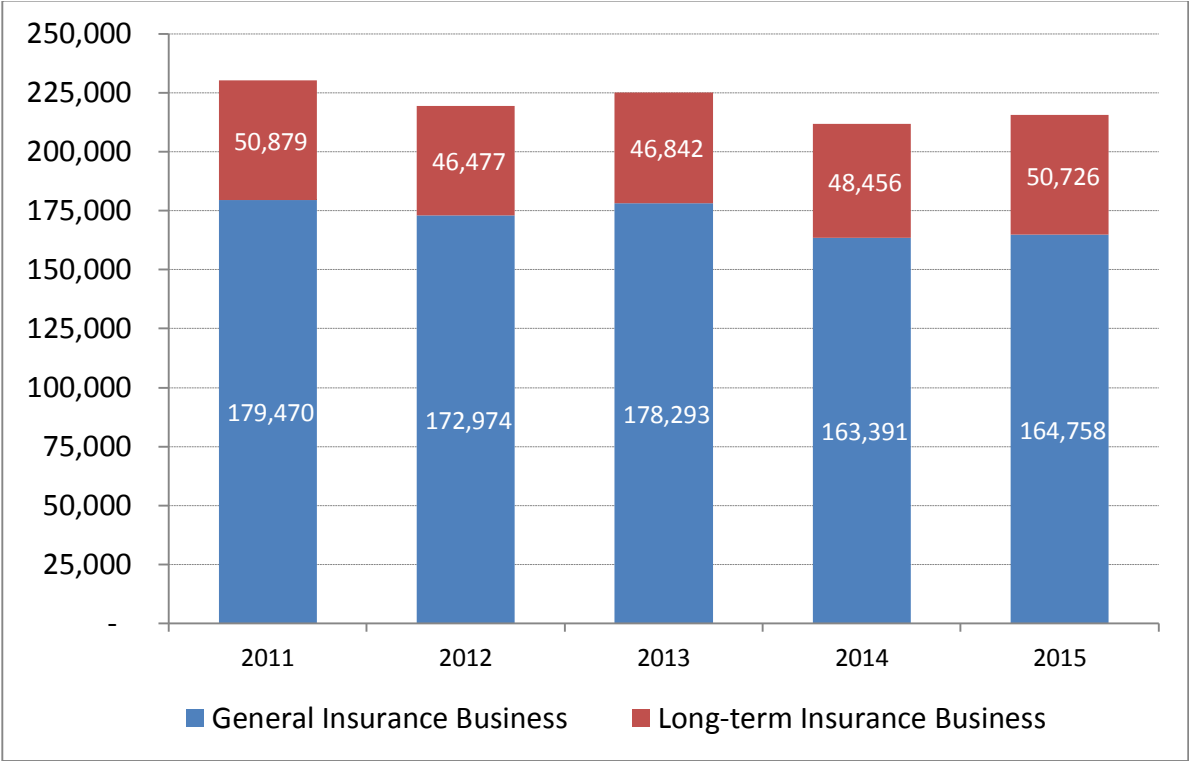
I will also update you on a couple of issues / policies.

# Insurance Sector Performance

## Written Premium

The insurance sector experienced growth of 1.7% in 2015 with total premium income increasing to EC\$215.5 million (2014: EC\$211.8 million). Figure 1 illustrates Gross Written Premiums by the industry over the last five years.

Figure 1: Gross Written Premiums

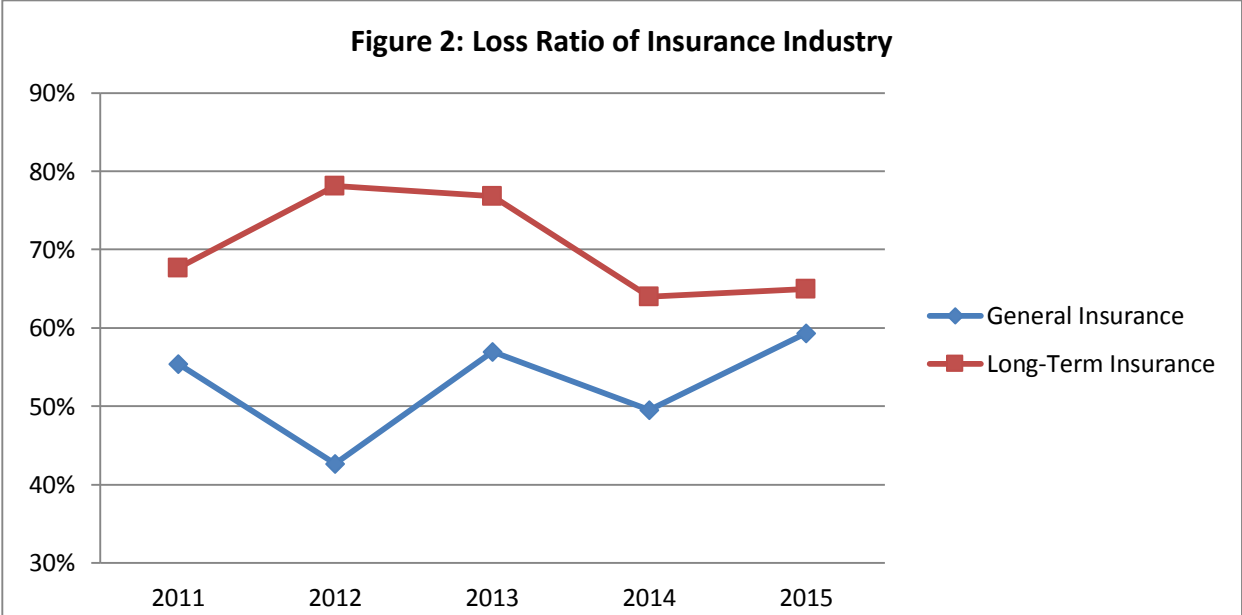


The increase experienced in gross premiums was largely due to the performance of the long-term class of business which grew by 4.5% (2015: EC\$50.7million; 2014: EC\$48.5million). There

was little movement in gross written premium in the general insurance sector which experienced a minimal increase of just 0.84 percent (2015 EC\$164.8 million; 2014: EC\$163.4 million). It is worthy to note that the marginal increase realized in general insurance business may not be a true reflection of the level of penetration experienced in this sector due to the downward trend in the unit price of insurance spurred by the highly competitive environment.

### Loss Ratio

The loss ratio is one of the indicators commonly used to evaluate the profitability of the insurance industry as it compares earned premiums to claims incurred by insurers. Figure 2 illustrates the Loss Ratio of the Insurance Industry over the last five years.

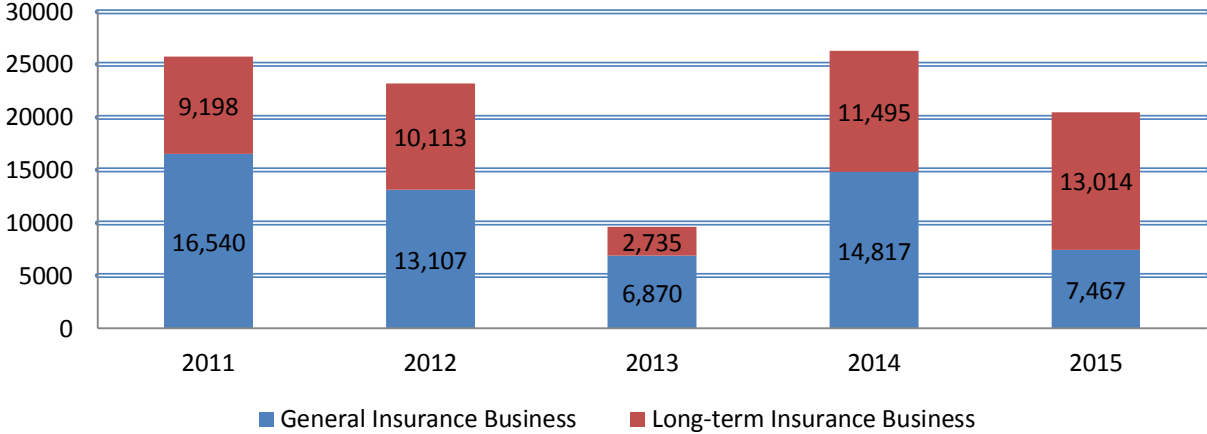


As can be seen, the loss ratio for general insurance business over the years is within the range of 40% to 60%. Long-term business is within a range of 65% to 80%. It is also evident that general insurance business exhibits greater volatility and the ratio is weakening over time. The long-term business exhibits less volatility and the ratio is moving in the opposite direction. There was little movement in the loss ratio of long-term insurers in 2015 over 2014. However, the general insurance sector experienced deterioration in its loss ratio which was fuelled by an increase in the amount of net claims. Analysis revealed that deficiencies in a few of the insurers' reinsurance treaty programmes contributed to the reported high net claims figure as some of the insurers recording significant losses recovered only a small percentage from reinsurers.

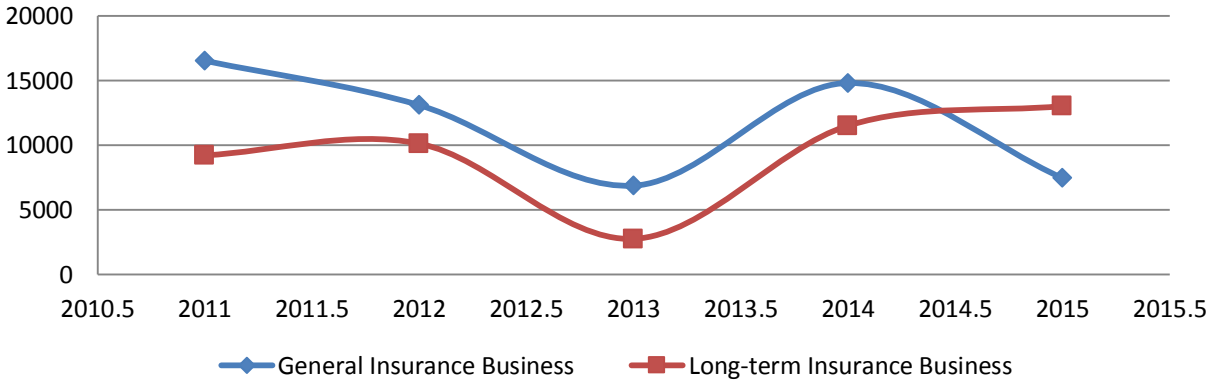
## **Net Income**

The industry experienced a significant decrease of 22% in net income (2014: EC\$26.31 million; 2015: EC\$20.48 million) due to significant claims incurred in the general insurance sector. Figure 3 and Figure 4 highlight industry net income over the last five years. Figure 3 illustrates the entire industry position while Figure 4 highlights the trend in performance for general and long-term business separately.

**Figure 3: Industry Net Income (\$'000)**



**Figure 4: Net Income General & Long-Term Business (\$'000)**

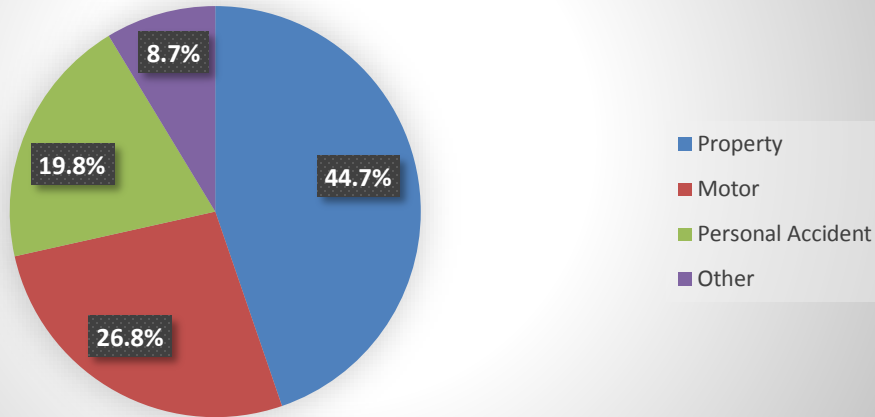


Prior to last year's drop in industry net income of general insurers, a similar dip was experienced in 2013 primarily due to the passage of a trough in December of that year which caused a spike in property insurance claims. This was followed by relatively low claims experience in 2014. The drop in the long-term insurers' net income in 2013 was primarily due to a decrease in investment income of a few of the major market players.

### **General Insurance Business**

The general insurance sector contributed 75.9% (EC\$164.8 million) of the total gross premiums in 2015. This amount includes business underwritten by Lloyd's Underwriters. Figure 5 illustrates class-wise general insurance business underwritten in 2015. Note that Lloyd's contribution is not included.

**Figure 5: General Insurance Business by Class**

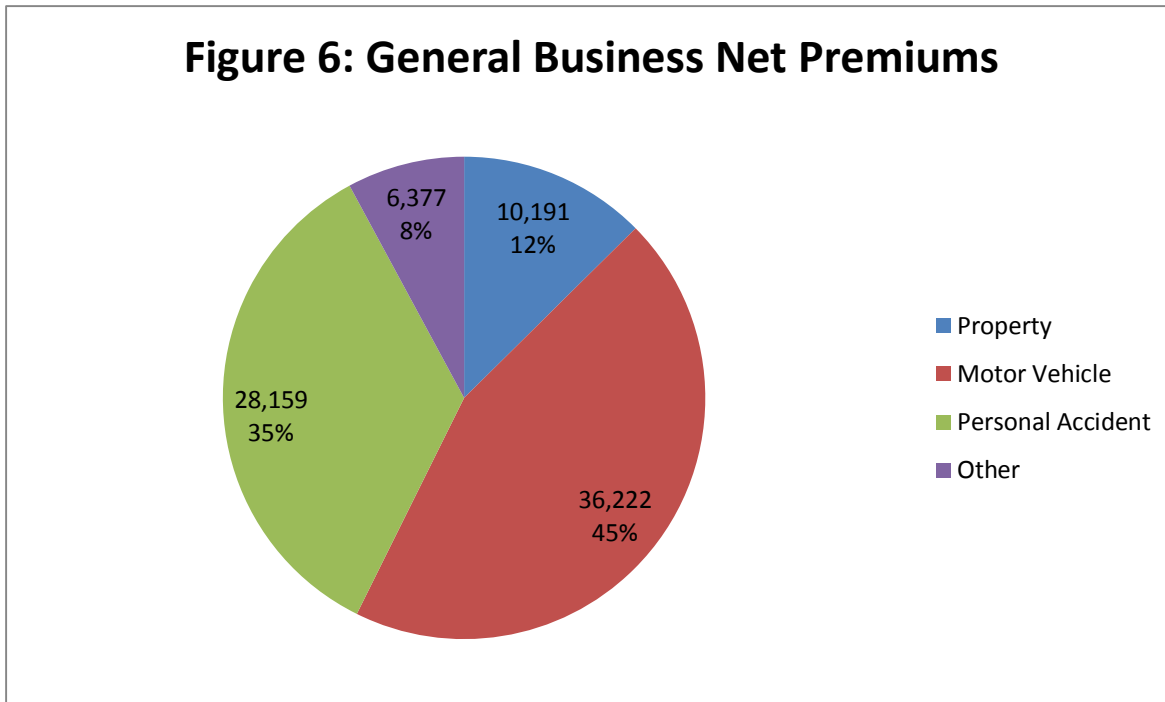


Property accounted for EC\$65 million (44.7%), motor vehicle EC\$38.9 million (26.8%), personal accident EC\$28.8 million (19.8%) while the three (3) other classes of general business (namely liability, pecuniary loss and marine, aviation and transport) accounted for EC \$12.6 million (8.7%) collectively.

### Reinsurance

The property class of insurance business continues to rely heavily on reinsurance with an average of 75% of premiums being ceded annually. As illustrated in Figure 6, in respect of net written premium, property insurance only accounts for 12% of general insurance business as compared to 45% of the market

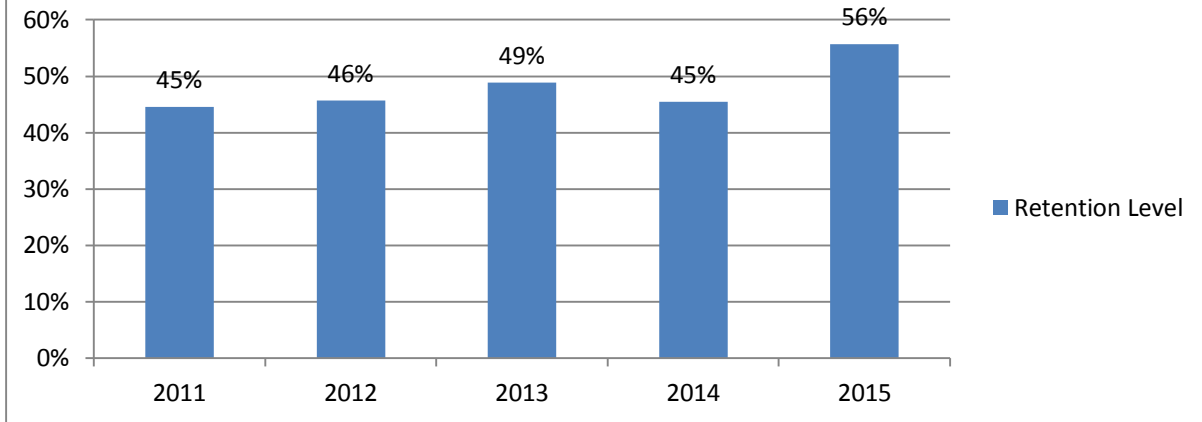
share in gross written business. Motor business and personal accident accounted for 45% and 35%, respectively.



However, as it relates to the general insurance sector collectively, the level of premium retention over the past few years has been increasing; as illustrated in Figure 7.



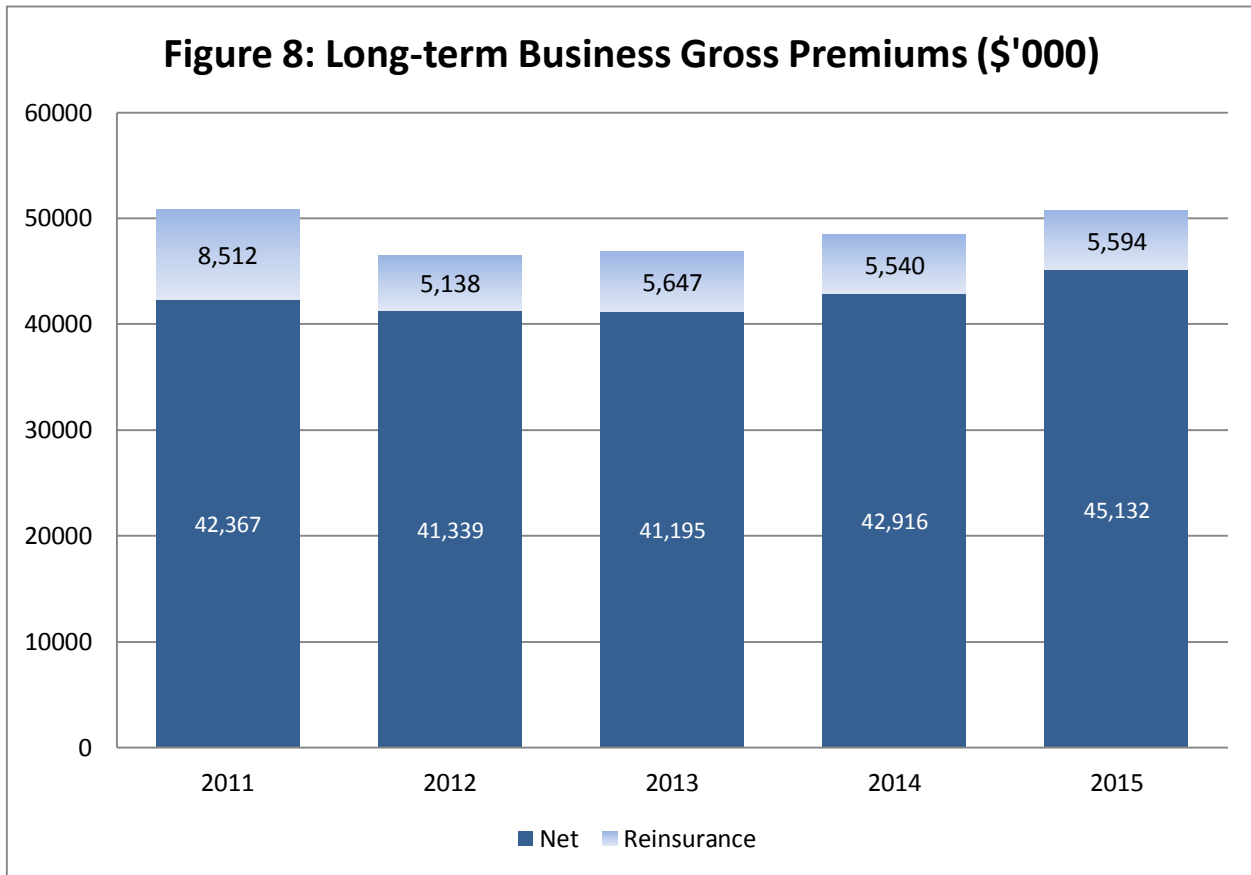
**Figure 7:  
General Insurance Premium Retention**



Save 2014, the level of retention has increased every year. There was a significant (11%) increase in the amount of premium retained by insurers in 2015, which for the first time in the last 5 years crossed the 50% mark.

## Long-Term Insurance Business

The long-term insurance sector has continued its upward trend in premium generation over the past years as illustrated in Figure 8.



The percentage increase from 2012 to 2015 stood at 9% (2015: EC\$50.7 million; 2012: EC\$46.5 million).

The long-term insurance classes of business (ordinary long-term, industrial life and annuities) demonstrate a low reliance on reinsurance over the last five years with an average of EC\$6 million or 12% being ceded annually.

The Regulators Office also thought it useful to provide industry with an update on its performance to date (i.e. based on companies' 2<sup>nd</sup> quarter submissions) and compare/contrast that information with the same period in 2015.

Based on the accounting submissions for each company's 2<sup>nd</sup> Quarter we are able to compare and present key performance indicators for the industry, namely, information in respect of Premiums, Underwriting Expenses and Profitability.

## Premiums

	2015-Q2 TOTAL GENERAL	2016-Q2 TOTAL GENERAL	2015-Q2 TOTAL LONG-TERM	2016-Q2 TOTAL LONG-TERM
1. Gross Direct Premiums Written	86,583	85,513	17,564	22,038
3. Reinsurance Ceded	42,019	36,967	1,119	2,735
<b>4. Net Premiums Written</b>	<b>44,564</b>	<b>46,545</b>	<b>16,445</b>	<b>18,388</b>

A few notable observations are made at first glance of the data:

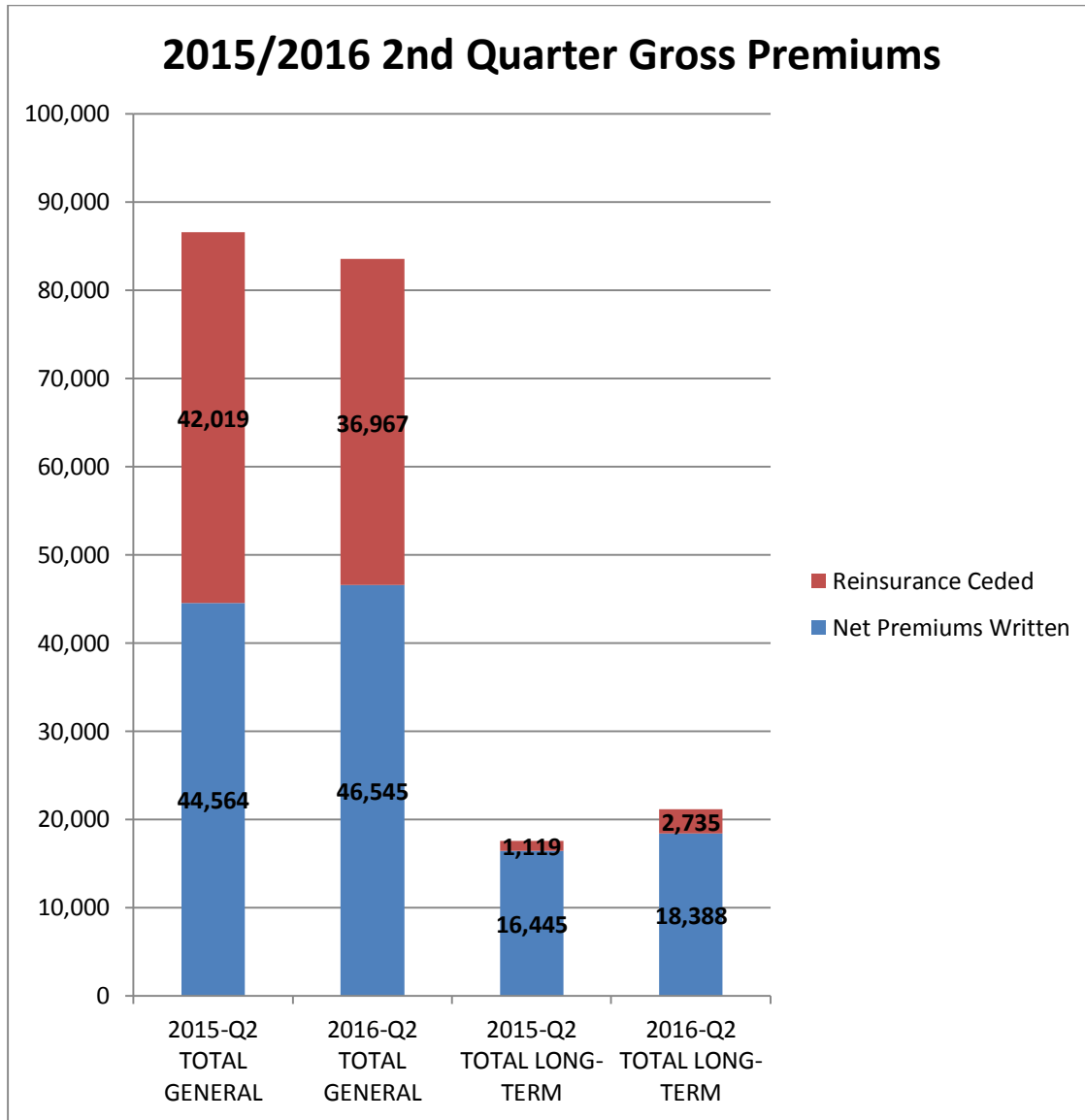
(1) In respect of the *General Insurance Classes* of business:

- Premiums generated **decreased** by \$3.07 Million or 3.55%.
  - Reinsurance ceded also **decreased**; however, by a greater percentage of 12.02% (\$5.05 Million)
  - Net Premiums **increased** by \$1.98 Million, which is equal to 4.45%.
- It thus appears that insurers are reducing reinsurance coverage as a measure to increase cash-flow.

(2) In respect of the *Long-term Insurance Class* of business:

- Gross premiums, Reinsurance ceded and Net premiums **increased** by 21%, 144% and 12%, respectively.

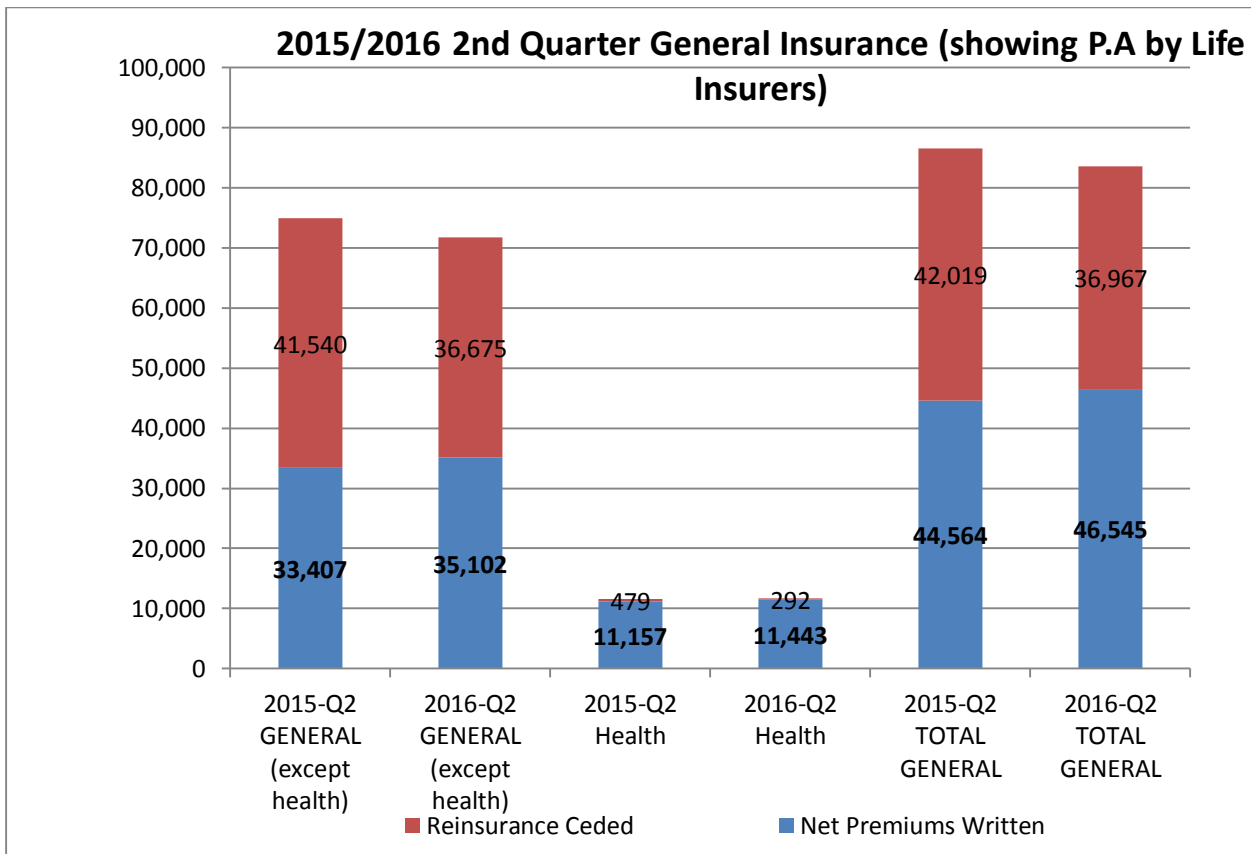
Viewed graphically, these observations are clearly highlighted.



### Composition of General Insurance Business

We also thought it useful to draw attention to something significant about the figures which comprise the General Insurance Business class.

While we are unable to provide information on the various classes of general insurance as was done in respect of the annual figures (this is not possible as the quarterly forms do not capture such information), information in respect of the Personal Accident Class underwritten by Life Insurers is being collected and was analysed.



The data shows that Personal Accident Insurance underwritten by Life Insurers account for approximately 25% of Net Premiums retained in the General Insurance class of business (2015-Q2: 25.04%; 2016-Q2: 24.58%).

Thus, General Insurers retention amounted to \$33.4 Million and \$35.1 Million in 2<sup>nd</sup> Quarter 2015 and 2<sup>nd</sup> Quarter 2016, respectively.

### 2015/2016 2nd Quarter Performance

In terms of profitability, our attention focused on premium income (earned premiums for general and net premiums for long-term), underwriting expenses, underwriting income/loss and net profit (before tax).

	2015-Q2 TOTAL GENERAL	2016-Q2 TOTAL GENERAL	2015-Q2 TOTAL LONG-TERM	2016-Q2 TOTAL LONG-TERM
Earned Premiums (general) / Net Premiums (long-term)	41,997	42,819	16,445	18,388
Total Underwriting Expenses	38,746	43,998	19,371	21,229
Underwriting Income (Loss)	3,251	-1,179	-2,875	-2,540
Net Profit (before Tax)	9,023	5,108	4,293	4,492

An increase in earned premium was recorded in both the total general classes of business and the total long-term classes of business in the 2<sup>nd</sup> Quarter of 2016 when compared to the same period in 2015. Underwriting expenses also increased in both class categories. However, in respect of the general class, underwriting expenses increased at a greater degree than earned premiums increased; resulting in an underwriting loss of

\$1.2 Million as at the end of the second quarter in 2016. There was also a reduction in Net Profit of \$4 Million (from \$9 million to \$5.1 Million).

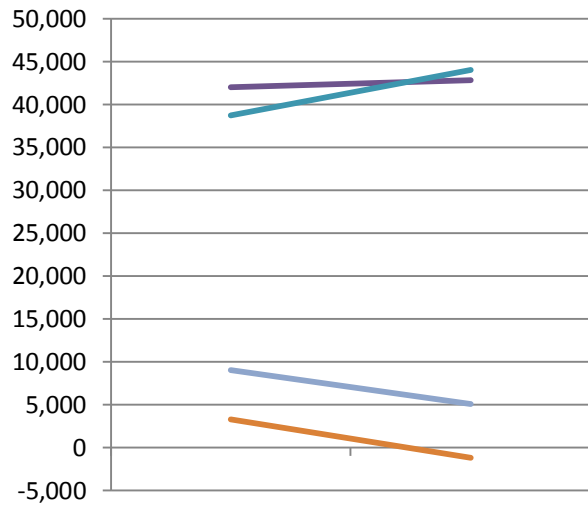
In respect of the long-term class, the increase in net premium of \$1.94 Million was greater than the increase in Underwriting Expenses of \$1.86 Million. Thus, there was a slight improvement in Underwriting Performance (2015 \$-2,875: 2016 \$-2,540) and Net Profit (2015 \$4,293: 2016 \$4,492) over the second quarter of 2015.

The turnaround in profitability from Underwriting Losses to Net Profit in the Life business is mainly attributable to investment income of \$6.75 Million and \$6.47 Million being recorded at the end of both periods in 2015 and 2016, respectively.

A comparison of the performance of the general classes of business and the long-term class is presented in the following graph.



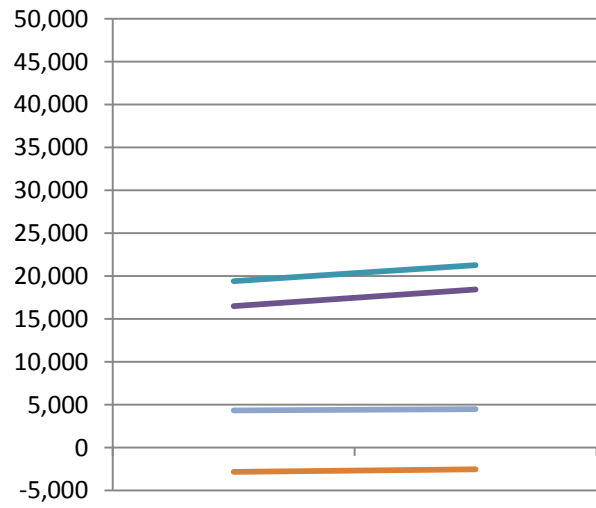
## General Insurance Business



2015-Q2 TOTAL GENERAL      2016-Q2 TOTAL GENERAL

- Earned Premiums
- Total Underwriting Expenses
- Underwriting Income (Loss)
- Net Profit (before Tax)

## Long-term Insurance Business



2015-Q2 TOTAL LONG-TERM      2016-Q2 TOTAL LONG-TERM

- Net Premiums (long-term)
- Total Underwriting Expenses
- Underwriting Income (Loss)
- Net Profit (before Tax)

## Pricing

Over the past few years the general insurance market has continued to grow increasingly competitive. Based on 2015 data, the HHI for the non-life sector was 786 points. In the face of increased pressure, companies have chosen to lower their premium rates, extend the terms and scope of cover offered, or weaken their underwriting selection criteria to protect their market position. This situation exists particularly in the property and motor classes of business. While this type of competition may provide cheaper insurance coverage for consumers, it also has detrimental consequences for companies' loss ratios and thus their bottom line.

Industry statistics on gross written premiums for the past few years suggest a highly competitive market. There are 19 insurers engaged in the underwriting of general insurance business other than health insurance. The record has shown a decline in general insurance business underwritten from \$178.3m in 2013 to \$163.4m and 164.8m in 2014 and 2015, respectively. The reduction in premiums written was experienced notwithstanding increases in the overall number of policies written by many of the insurers. Insurers have also reported that some clients are reducing their level of cover in respect of property insurance and persons are increasingly opting for third party motor insurance rather than comprehensive coverage. The claims

environment has also been challenging especially in the motor insurance sector which has led to companies increasingly adopting what appears to be delay tactics in dealing with claimants. All of these aspects have the potential to increase the risk of mispricing business and/or weakening the reserving basis below what is adequate.

In this challenging environment, companies must not let their guards down. I implore you to be mindful of the importance of good underwriting practices and guard against the temptation of taking a short term view at your own peril. I wish to remind you, as I am sure you are quite aware, that at the forefront of the most common causes of insurance failures are underpricing and under-reserving.

Insurance is a volume business, and given the small size of the market, the continued reduction in the price of insurance could be catastrophic for some insurers. The soft insurance market has sparked the debate for rate regulation. The question is then; should the market be allowed to continue to dictate its own prices? Or, should the regulator impose price restrictions?

In developed markets such as the USA and Canada, the regulators have had to impose rate regulations on property and casualty insurance but for very different reasons. The main

thrust of such an approach was to facilitate inclusive insurance, in particular where insurance is mandatory such as motor third party insurance.

We believe that this subject is worthy of discussion and the regulator's office will be seeking to engage the industry on this issue in the not too distant future.

I also like to take the opportunity to speak briefly on a subject which I believe is connected to the topic of pricing; i.e. insurance coverage for mini-buses. Information reaching us suggests many of the operators in the market refuse to offer insurance coverage for mini-buses. Presumably, this action is influenced by:

- i. The very high associated risk by this segment; and
- ii. The highly competitive, if not non-representative pricing of this risk.

But third party risk coverage is a mandatory requirement of law and therefore M-Plate operators must be so covered. In the circumstance, right-pricing of the risk takes added significance and industry partners must find an appropriate resolution to this problem.

While it is important to exercise discipline in your underwriting selection criteria for mitigating your risks, the exclusion of an entire group could well be considered as being discriminatory; and if I might add unreasonable to expect only the handful of indigenous entities to bear this burden.

For jump starting this debate, I wish to remind you that the privilege of conducting motor business in the market carries with it an obligation to offer risk cover on all segments of our transportation system.

## **Reserving**

The subject of reserving is of paramount importance for the regulator's office. I will therefore dissect this topic by examining life and general insurance businesses separately.

## Life Insurance

Each Life Insurer is required by law to conduct an actuarial valuation of its book of business; however, the method of actuarial valuation is not prescribed in legislation. Therefore, insurers are not restricted in their choice of valuation method. However, the ultimate goal is for companies to value their

liabilities adequately and the Insurance Act, though it does not prescribe the method of valuation, mandates that no policy should be counted as an asset. What this means, is every single policy should be valued and where there is a negative reserve, the policy must be valued at zero. This is a very important requirement, and close attention is paid to this requirement when reviewing Actuarial Valuation Reports especially in the case of creditor or term life insurance.

Additionally, International Financial Reporting Standards (IFRS) mandates that insurance liabilities must be actuarially valued annually. Again, the standard does not currently address the issue of which valuation method is to be applied by the Actuary. As different methods may yield different results the issue of comparability amongst companies remains a concern for the regulator's office.

Having said this however, the majority of companies utilized the Policy Premium method, which is the preferred method by the Caribbean Actuarial Association (CAA). The regulators in the Caribbean region have been in discussion with the CAA regarding the establishment of a single standard methodology for the valuation of insurance liabilities. This will address the issue of cherry picking and allow for greater comparability amongst companies.

## Assumptions

Another area of key importance in the actuarial valuation of liabilities is the assumptions made by the actuary. Minor changes in interest rates, discount rates, persistency, morbidity and mortality could significantly impact the liability position of a company. The regulator's office, in the recent past, has had reason to question the adequacy of reserving of some companies. The auditors too have a part to play in ensuring that the insurance reserves are adequate and must discuss their concerns with the appointed actuary. We have observed situations where the number of policies and the sum assured of companies have continued to increase significantly while the insurance liabilities declined. While it may not necessarily be a case of deliberate under-reserving, questions must be asked, and the regulator must be duly satisfied that the reserves are adequate.

Do note that where serious deficiency concerns arise, as Regulator and in keeping with statute, the FSRA will require an independent actuarial review at the expense of the insurer.

The importance of adequate reserving cannot be overstated as it has many implications for the company and its policyholders. The Insurance Act requires a life insurance company to establish an insurance fund equal to its policyholders' liabilities. The

under-reserving of liabilities therefore means that the policyholders are exposed as the company would not be in a position to meet its liabilities when they fall due. Also, under reserving may lead to significant profit volatility when sudden increases in provisions must be made in subsequent years.

## General Insurance

Until recently, actuarial valuation of non-life insurance liabilities was not mandatory. IFRS 4 now requires all insurance companies to have a liability adequacy test done to verify whether the liabilities are adequately provided for. The regulator's office requires every company to submit with their annual statutory returns an actuarial certification confirming the adequacy of its insurance liabilities. The certification from the Actuary should provide a level of comfort to the regulator that the reported liabilities are materially correct. However, the regulator's office has also had reasons to question some of the significant decreases experienced in liabilities on the books of some companies.

The regulator's Office understands that in the case of general insurance, the liabilities could be significantly more volatile, considering the nature of the business and depending on the



reinsurance arrangement of the company. However, to facilitate the regulator's assessment of the reserves, the claims experience Forms (C15) must be duly completed by every insurer for each class of business conducted.

Our analysis of the information reported on these Forms has in some instances revealed patterns of significant under-reserving or what appear to be delays in the reporting of claims on the books of some insurers. There have also been cases where the explanations for unusual drops in the claims experience are attributed mainly to the expiration of the statute of limitations resulting in the removal of the provisions on the books of the companies. The regulator's office will be paying closer attention to these issues to ensure that loopholes in the claims provisioning process are not exploited by companies.

The regulator has also noticed a pattern by some companies of failing to adequately populate the claims experience Forms. We have in the past provided assistance by way of training to companies' accounting staff and have continued to offer our assistance in that regard. However, while we have seen some improvements in the completion of these Forms, some companies continue to either, leave-out important information, or simply complete the Forms incorrectly. As stated earlier, the Forms serve as a very important tool in monitoring the reserving pattern of companies. Thus, the regulator's office will deem the

submission of your accounts incomplete should you fail to provide duly completed Claims Experience Forms with your submission. The regulator's office remains open to providing clarification or assistance to anyone who requires any clarification or assistance for completing those Forms.

I call upon directors and management of companies to take their responsibility and obligation for ensuring the adequacy of reserving very seriously. The FSRA therefore expects insurers to have a robust approach to the setting of reserves and to put in place appropriate and adequate oversight of reserving processes. More specifically, Insurers are expected to:

- understand the key issues and sources of material uncertainty in the reserve-setting process, and how these may impact the reserving basis, in order to make informed decisions on reserve levels;
- assess whether an unexpired risk provision needs to be established. This is of particular relevance, considering the current market conditions;
- have regard to data quality and consider how any data limitations might impact companies' reserves

- ensure that the level of reserving strength is monitored overtime so that appropriate and timely action can be taken if necessary

## **Developments in Regulation and Supervision**

- Risk-based Assessment

In the FSRA's presentation at last year's AGM, you were advised of the intention to introduce risk-based assessment to the supervision toolkit. We are pleased to report that with the assistance of the Caribbean Regional Technical Assistance Centre (CARTAC) the FSRA has developed a risk-based assessment framework which includes a risk-based matrix developed to assist in the assessment of the risks of registered entities. We are still in the early stage of applying this form of assessment. Although

this tool was developed for aiding the regulator's internal assessment processes, we believe that companies can benefit directly from its use. It is our intention therefore to make this risk matrix available to companies in the future. This will not only help companies in assessing their own risks but companies will now have a better understanding of how the regulator assesses them. The ultimate goal is for companies to perform their own risk assessment and submit together with their annual returns.

- ***Insurance Appeals Tribunal Regulation***

In collaboration with the ICSL, Regulations have been drafted to strengthen and support the provisions in the Insurance Act relating to the Appeals Tribunal. We are hoping that the regulations will be enacted before year end.

- ***Plan of Arrangement (BAICO) Bill***

The Judicial Managers for British American Insurance Company (BAICO), through their continuous efforts, have been able to secure some additional funds for the benefit of all policyholders and intend to make a partial payment to the policyholders in the near future. However, in order to distribute the funds to policyholders they have indicated that in the absence of a special arrangement there would need to be separate liquidation processes for each branch in each jurisdiction which will be a highly inefficient, costly and a confusing process for policyholders; resulting in the further dilution of the distribution to policyholders.

In that regard the enactment of a Plan of Arrangement Bill has been proposed and it is anticipated that this Bill will soon be enacted. The necessary changes are being made to the bill in order to tailor it to meet the requirements of Saint Lucia.

In closing, I take the opportunity to commend the Council on the important role that it continues to play in the insurance industry. The regulator's office remains committed to working with the industry as we strive to enhance and maintain the reputation and integrity of the Sector for the benefit of all stakeholders.

I thank you!