

ADOPTION OF RISK-BASED CAPITAL FRAMEWORK FOR THE PHILIPPINE MUTUAL BENEFIT ASSOCIATIONS

IC INSURANCE MEMORANDUM CIRCULAR NO. 11-2006, December 08, 2006

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To establish the required amounts of members' equity to be maintained by mutual benefit associations (MBAs) in relation to their investment and insurance risks, the Insurance Commission, after consultation with the MBAs hereby approves the adoption of the Risk-Based Capital (RBC) Framework and issues the following rules and regulations pursuant to the powers vested in me by the provisions of Section 414 of the Insurance Code.

I. RBC Ratio and Members' Equity

The investments and insurance risks of the MBA shall be classified under four (4) major categories.

- Asset Default Risk, denoted by C-1;
- Insurance Pricing Risk, denoted by C-2;
- Interest Rate Risk, denoted by C-3; and
- General Business Risk, denoted by C-4.

The RBC requirement is given by the formula:

$$\text{RBC Requirement} = \sqrt{(C1 + C3)^2 + C2^2} + C4$$

The RBC ratio of the MBA shall be calculated as Members' Equity divided by the RBC requirement as determined in accordance with RBC Exhibit Instructions and Disclosures (See Annex A[*]).

"Members' Equity" is defined as Admitted Assets minus All Liabilities inclusive of Actuarial Reserves and other obligations under the policies and membership certificates.

Every MBA is annually required to maintain a minimum RBC ratio of 100% and not fail to the Trend Test as stated in (II.A.2) below.

II. Levels of Regulatory Intervention

The following levels of regulatory intervention then follow based on this ratio:

RBC Ratio = Y Event Description

$$100\% < Y < 125\%$$

Trend Test

Linear extrapolation if next year's ratio <100%. If so, move to MBA Action Event.

$$75\% < Y < 100\%$$

MBA Action

Submit RBC plan and financial projections. MBA implements the plan.

$$50\% < Y < 75\%$$

Regulatory Action

IC Authorized to examine the MBA and issue Corrective Orders.

$$35\% < Y < 50\%$$

Authorized Control

IC Authorized to take control of the MBA.

$$Y < 35\%$$

Mandatory Control

IC required to take control of the MBA.

A. MBA Action Event shall refer to any of the following events:

- The RBC ratio of the MBA is less than 100% but not below 75%, or
- The Trend Test has failed, which shall occur in the event that:
- The RBC ratio is less than 125% but is not below 100%,

- The RBC ratio has decreased over the past year, and
- The difference between RBC ratio and the decrease in the RBC ratio over the past year is less than 100%

A.1 In the event of the MBA Action Event, the MBA shall file to the Commissioner within forty-five (45) days of the event a RBC plan that shall:

- Identify the conditions that contributed to the event;
- Contain proposals of corrective action that the MBA intends to take and that would be expected to result in the elimination of the event;
- Provide projections of the MBA'S Annual Statements for at least two (2) years with and without the proposed corrective actions; including but not limited to projections on the balance sheets, analysis of operations (total), surplus accounts, RBC Exhibits and lines of business information relevant to the RBC plan;
- Identify the key assumptions impacting the MBA's projections and the sensitivity of the projections to the assumptions; and
- Identify the quality of, and problems associated with, the MBA's business, including but not limited to its assets, anticipated business growth, surplus strain, extraordinary exposure to risk, mix of business and use of reinsurance, if any, in each case.

The Commissioner shall notify the MBA within sixty (60) days upon submission of the RBC plan whether it shall be implemented or is unsatisfactory. In the latter case the Commission shall include reasons for the determination and proposed revisions to the RBC plan, and the MBA shall resubmit the RBC plan within thirty (30) days of notice.

B. Regulatory Action Event shall refer to any of the following events:

- The RBC ratio of the MBA is less than 75% but not below 50%; or
- The MBA fails to submit a RBC plan satisfactory to the Commissioner, if any, within the filing deadline; or
- The Commissioner notifies the MBA of its failure to adhere to its RBC plan, and wherein the failure shall adversely affect the MBA's ability to eliminate the MBA Action Event in accordance to its RBC plan.

B.1 In the event of a Regulatory Action Event, the Commissioner is authorized to

- Require the MBA to submit a RBC plan within forty-five (45) days of the event;
- Perform such examination or analysis, as deemed necessary, of the MBA's accounts, operations and RBC plan; and
- Subsequent to the examination or analysis, issue a Corrective Order specifying corrective actions the MBA is required to undertake.

The Commissioner may retain actuaries and other consultants as necessary to re- view the MBA's accounts, operations and RBC plan and to formulate the necessary corrective orders, the fees and costs of which shall be borne by the affected MBA.

C. Authorized Control Event shall refer to any of the following events:

- The RBC ratio of the MBA is less than 50% but not below 35%; or
- The Commissioner notifies the MBA of its failure to satisfactorily respond to a Corrective Order as stated in

(B.1.c).

In the event of an Authorized Control Event, the Commissioner is authorized to place the MBA under regulatory control under Sec. 247 of the Insurance Code, should the Commissioner deem it to be in the best interests of the MBA's members and creditors and of the general public. The Authorized Control Event shall be deemed sufficient grounds for the Commissioner to take action under Sec. 247 of the Insurance Code.

D. Mandatory Control Event shall occur if the RBC ratio of the MBA is less than 35%. Should this event occur, the Commissioner is required to place the MBA under regulatory control under Sec. 247 of the Insurance Code. The Mandatory Control Event shall be deemed sufficient grounds for the Commissioner to take action under Sec. 247 of the Insurance Code.

III. Submission of the RBC Exhibits and Items

Every MBA shall annually accomplish and file the relevant RBC Exhibits and Items that shall form part of the Annual Statements in accordance with the instructions provided.

IV. Confidentiality

With the exception of the RBC Exhibits that shall form part of the Annual Statements, all other disclosures and RBC Plans filed with the Commissioner shall be kept confidential in the same manner as the Annual Statement Schedules and other confidential reports required by the Commission.

V. Compliance with the Guaranty Fund, Reserves Liability and RBC Requirements

The MBA shall, in addition to the Guaranty Fund required under Insurance Memorandum Circular Nos. 2-2006 or 9-2006 and Reserves Liability required under Section 397 of the Insurance Code, comply with the RBC requirement.

VI. The RBC Framework shall be subject to review at least once every three (3) years.

The Insurance Commission may issue such other guidelines as it deems necessary to enforce the provisions of this Circular. Non-compliance with this Circular and any additional guidelines shall result in the revocation of the MBAs certificate of authority.

This Insurance Memorandum Circular shall take effect immediately.

Adopted: 8 Dec. 2006

(SGD.) EVANGELINE CRISOSTOMO-ESCOBILLO

Insurance Commissioner

[*] Text Available at Office of the National Administrative Register, U.P. Law Complex, Diliman, Quezon City

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