



**Financial Services
Commission**

Insurance Guidance Note No. 2C
Insurance Companies Ordinance 1987
The Use And Preparation Of Abbreviated Annual
Returns For Captive Insurers

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Introduction

1. Following discussions with representatives of the insurance industry, the Commissioner of Insurance (the "Commissioner") has agreed to allow a certain category of Gibraltar insurers - namely, captive insurers which do not transact a significant amount of third party business - to report their business by means of abbreviated returns (i.e. the CAP returns). The forms to be used – the CAP forms – are at Annex 4.
2. The CAP returns which the Commissioner has agreed to accept, and the specific guidance that goes with them, are below. The CAP returns were designed to lessen the burden of reporting for captive insurers, mainly in terms of fewer forms to be completed, whilst not departing significantly from the standard reporting format prescribed in the Insurance Companies (Accounts and Statements) Regulations 1998 (the "Regulations"). (Except where stated to the contrary, references in this Guidance Note to "regulations", "paragraphs" and "Schedules" relate to the Regulations). The Regulations remain appropriate to the new forms as does the full guidance note, Insurance Guidance Note 2A, and persons responsible for the preparation, signing and audit, of the CAP returns will need to have referred to both before preparing, signing or auditing, them.
3. There will be no automatic right to use the CAP forms. They will be available only to captive companies (or their managers) who have applied to the Commissioner asking him to use his powers under section 113 of the Insurance Companies Ordinance 1987 ("the Ordinance") to provide a dispensation enabling the company to use the CAP returns rather than the full returns prescribed under the regulations. In making the application, the companies should identify the circumstances which would justify the concession. Generally speaking, these circumstances will be that the company is a captive insurer which has no significant third party business. Unless he provides the necessary section 113 dispensation, the Commissioner will continue require all returns to him to be made as prescribed by the Regulations.
4. The following paragraphs contain guidance on how to complete the CAP returns. This document is included in the Commissioner's list of published guidance to which he expects companies to certify compliance under the provisions of paragraph 5 of Schedule 6 to the Regulations.

Completion of Forms

5. The first Form in the return (CAP 1) should be signed by the two signatories required.

Currency

6. All forms are to be completed in sterling, with
 - assets and liabilities converted at the financial year end exchange rate, and
 - income and expenditure converted using "such basis of conversion as are in accordance with generally accepted accounting practice".

If an insurer wishes to complete returns in any other currency, the Commissioner will consider a request for a dispensation under section 113 of the Ordinance.

Presentation of amounts

7. All amounts in the forms should be shown in units of 1,000 rounded to the nearer 1,000.



Comparative amounts and brought forward amounts

8. Columns are included on Forms CAP 1 to CAP 6 and CAP 10 for the disclosure of comparative amounts for the previous financial year. These amounts should be reported as stated in the previous return (after any correction required to be made under s52(5)), but without restatement for any prior year adjustment even where such restatement is permitted under generally accepted accounting practice. In the first year that abbreviated returns are used, it may be necessary to restate amounts. Therefore, when any brought forward amounts is restated, the reason for the restatement must be given in a supplementary note to the Form upon which the brought forward amount appears.

Supplementary Notes

9. Supplementary notes should not be shown on the face of a Form but should be shown on a separate sheet or sheets of paper. It would be helpful if the notes for all Forms are bound together towards the end of the return (but before the certificates) and not interleaved with the Forms to which they relate.
10. Each note is given a unique reference code (the first 2 digits of the code are the number of the Form and the final two digits the number of the note).
11. Where an insurer wishes to include an extra note (beyond those required to be included), it should identify the form and give the next unused sequential code number for that form.

Forms CAP 1 To CAP 6

CAP 1 – Statement of net assets and solvency

Completion of the Form

12. Amounts included in lines 14 and 15 shall be determined in accordance with regulation 4 of the Insurance Companies (Solvency Margins and Guarantee Funds) Regulations 1996 (the "Solvency Margin Regulations"), or as specifically allowed pursuant to an order issued under section 113 of the Ordinance. These lines show 2 types of liability which are taken into account in net admissible assets but which, provided that net admissible assets are not negative, may (to a limited extent) be added-back for the purpose of determining whether the company meets its required margin of solvency.
13. Lines 31 to 39 reconcile the balance of net assets (line 23) brought forward and carried forward. The brought forward amount shown at line 31 should not be restated for any reason.
14. The two most frequent reasons for a movement in net assets are listed respectively at lines 32 and 33. They are:
 - the retained profit or loss for the financial year (CAP 6.59.1),
 - movements in the difference between the value of assets under the Insurance Companies (Valuation of Assets and Liabilities) Regulations 1996 (the "Asset Valuation Regulations") and under the GAAP valuation rules – CAP 4.Line 33 shall be equal to CAP 4.92.2 to CAP 4.95.2 less CAP 4.92.1 to CAP 4.95.1.
15. Movements in the net assets which are not attributable to the two reasons given above should be included at line 34 and explained by way of supplementary note to the Form.
16. The abbreviated return should be signed at the foot of CAP 1 by the required signatories.

Supplementary Notes

17. Four supplementary notes are required -
- (i) [Code 0101] – Where a section 113 Order has been issued disapplying or modifying any of the provisions of the Regulations (including preparation of the abbreviated returns), a note to CAP 1 explaining the effect of the order is required.
 - (ii) [Code 0102] – In addition to the reconciliation of balance of net assets brought forward and carried forward, which appears on the face of CAP 1, a further reconciliation, which takes net assets as per the Annual Return and reconciles them to the net assets as they appear in the statutory accounts is required by way of supplementary note.

The reconciliation is between line 99 of CAP 4 less line 59 of CAP 5 and the amount shown under balance sheet item A “capital and reserves” in the company’s accounts.
 - (iii) [Code 0103] – Particulars of any “other movements” shown at line 34.
 - (iv) [Code 0104] – Particulars of any section 113 order allowing subordinated loan capital not to be treated as a liability for the purposes of determining whether the insurer holds net assets which match its required margin of solvency – the requirement for this note will be specified in the section 113 order itself.

CAP 2 and CAP 3 – Calculation of required margin of solvency

CAP 2 – the First Method: the premium basis

18. Lines 11 and 22: determine the gross premiums receivable and gross premiums earned in the financial year.
- (a) “Gross premium” is defined as “premiums after deduction of discounts, refunds and rebates of premium, but before deduction of premiums for reinsurance ceded and of commission payable”. It includes premiums receivable from reinsurance contracts accepted by the insurer. This has the same meaning (subject to one important exception described in sub-paragraph (c) below) as “gross premiums written” as it occurs in the other forms in the Regulations. The amount of “gross premium” to be taken is limited by the words “receivable” and means “recorded in the company’s books as due to the company in respect of risks incepted in the financial year”. Policies transferred to an insurer under a Schedule 10 transfer (or a transfer under the equivalent law of an EEA State) should be considered to be incepted on the date of transfer.
 - (b) In effect, therefore, (subject to the exception described in (c)), “gross premiums receivable” may be treated as being the same as that portion of “gross premiums written” which is in respect of risks incepted in the financial year. This may be derived from the other Forms in the abbreviated return as follows: take the sum of the entries in columns 1 and 2 for lines 13 to 15 on all forms CAP 11 and of the entry at line 11 for the current underwriting on all forms CAP 14.
 - (c) The exception occurs where premiums receivable are excluded from gross premiums written as shown in CAP 11 and CAP 14 by virtue of the rule in paragraph 25 of Schedule 2 to the Regulations. This says that “amounts in respect of inwards and outwards contracts of insurance shall be classified for inclusion in Forms INS 20 to INS 39 according to their economic substance in accordance with generally accepted

accounting practice". This, in effect, means that the accounting treatment for so-called financial reinsurances is to be the same as in the statutory accounts. The point to note here is that even where, under this rule, the consideration receivable under a contract of insurance is not classified as "gross premiums written" for the purposes of those forms, it must be included as "premiums receivable" on CAP 2. The CAP 2 "premiums receivable" should include all considerations receivable in respect of contracts which constitute carrying on insurance business under the Ordinance.

19. Lines 12 and 23: deduct premium taxes and levies, but only to the extent that: (i) in the case of taxes, they are included in premiums and (ii) in respect of levies, they are related to premiums and are "recorded in the company's books as payable in the appropriate financial year or years in respect of general business". Under generally accepted accounting practice, IPT is excluded from the amount shown for premiums and should not be deducted at line 12 on the Form. The Financial Services Compensation Scheme levy in respect of business written or earned during the year may be deducted but only to the extent that a provision for that anticipated liability has been established.
- 19A. Lines 14 and 15: statistical methods may be used to allocate the premiums in respect of classes 11, 12 and 13.
20. Lines 16 and 27: adjust the sub-total derived from the above to an annual figure if the financial year runs for more or less than 12 months.
21. Lines 17 to 20 and 28 to 31: (i) analyse the amount arrived at in lines 16 and 27 between "other" and "health insurance based on actuarial principles"; (ii) in the case of each amount, if appropriate, divide into two portions of up to 50 million Euro and the excess over 50 million and (iii) apply the appropriate percentages (18, 16, 6 or 51/3, as the case may be) to the totals arrived at and add together the resultant sums to determine Sub-total B. The Commissioner will advise, if requested, whether business carried on under a particular policy falls within the definition of "health insurance based on actuarial principles". The £/Euro rate of exchange to be used is that prevailing at the previous 31 October and is advised to insurers each year.
22. Lines 41 to 46: Determine (i) gross claims paid in the relevant period of 3 financial years; (ii) gross claims outstanding carried forward; and (iii) gross claims outstanding brought forward. Determine the gross claims incurred, Sub-total C, as (i) plus (ii) less (iii).
- (a) "Claims paid" and "claims outstanding" are defined in detail in the Solvency Margin Regulations. In essence, they refer to the amounts recorded in the company's books as -
- "paid in full or partial settlement of" or "set aside as likely to be sufficient to meet" claims under contracts of insurance; or as
 - expenses "incurred" or "set aside" as likely to be incurred which are "directly attributable to the settlement of individual claims"; less
 - related salvage recoveries, recoveries from third parties and recoveries from other insurers (but not reinsurance recoveries).
- (b) The definition of "claims outstanding" includes the provision for claims incurred but not reported.

- (c) In effect, although the Solvency Margins Regulations do not express themselves in these terms, the above definitions of “claims paid” and “claims outstanding” are equivalent (subject to one important exception described in (f)) to the corresponding amounts included in CAP 12 and CAP 15, but excluding the “claims management costs”.
 - (d) For “claims paid”, the equivalent amount is the sum of the amounts at lines 11 and 15 in column 2 in all forms CAP 12 and of the amounts at line 21 of the total column in all forms CAP 14.
 - (e) For “claims outstanding” the equivalent amount is the sum of the amounts at lines 11 and 15 in column 3 in all forms CAP 12 and of the amounts at lines 11 and 13 of the total column in all forms CAP 15. For an insurer which discounts its claims outstanding, this requires that the undiscounted provision be taken. If necessary the brought forward amount (here and on Form INS 4) should be restated as undiscounted.
 - (f) The exception arises for the same reason as described in paragraph 1(c) above. Amounts are classified for inclusion in CAP 12, CAP 14 and CAP 15 according to their economic substance in accordance with generally accepted accounting practice. However, in CAP 2 and CAP 3, “claims paid” and “claims outstanding” should include all amounts “paid” or “set aside” for claims under contracts which constitute carrying on insurance business under the Ordinance, even where such amounts are not classified as “claims paid” under generally accepted accounting practice.
23. Lines 47 and 48: determine the net claims incurred, Sub-total D, by deducting from the gross claims incurred, Sub-total C, the total sum recoverable in respect of that amount under reinsurance contracts ceded. Line 47 should only include amounts classified for inclusion as reinsurance in CAP 12, CAP 14 and CAP 15 according to their economic substance in accordance with generally accepted accounting practice (except that where gross premium has been included in line 11 only by virtue of paragraph 5(f), all reinsurance of that gross premium (whatever its economic substance) may be included in sub-total C.
24. Line 49: determine the First result by multiplying Sub-total J by the ratio of Sub-total D to Sub-total C, (or if that fraction is less than one half, by one half; or if the fraction is more than one, by one).

CAP 2 – (the brought forward amount)

- 24A. The provision for claims outstanding shown in line 50 are to be net of reinsurance. The guidance in paragraphs 22 and 23 applies, except that despite 22(e), claims that are discounted will not need to be restated as undiscounted if they are in respect of class 1 or 2 business or for annuities or if the insurer is a pure reinsurer that does not have permission to effect contract of insurance. The brought forward amount in line 51 is then the lower of the required margin of solvency that applied during the financial year in question and that amount multiplied by the ratio of claims outstanding at the end of that financial year to the claims outstanding at the beginning of that financial year.

CAP 3 – the Second Method: the claims basis

25. Line 11: Determine the reference period. If an insurer has not been in existence long enough to acquire a reference period, this should be indicated by entering a zero at the box in line 11 and lines 21 to 41 ignored. For the majority of insurers, the reference period will be the last three financial years.
26. Lines 21 to 29: Establish the amount of “claims incurred” to determine Sub-total E in a similar way to that explained in paragraph 22 above. For example,

where the reference period is the last 3 financial years, the claims incurred should be derived (from the formula described in para 22) from the amounts reported in the returns for those last 3 years. However, it is acceptable to restate amounts of "claims incurred" for currency movements. Claims, provision and recoveries in respect of classes 11, 12 and 13 must be increased by 50%. Statistical methods may be used to allocate the claims, provisions and recoveries in respect of these classes.

27. Line 31: Reduce the sum derived to an annual figure by multiplying by 12 and dividing by the number of months in the reference period, to get Sub-total F.
28. Lines 32 to 39 (i) analyse Sub-total F between "other" and "health insurance based on actuarial principles"; (ii) in the case of each amount, if the amount is more than 35 million Euro, divide into two portions of up to 35 million Euro and the excess over 35 million Euro and (iii) apply the appropriate percentages (26, 23, 82/3, 72/3, as the case may be) to the totals arrived at and add together the resultant sums to determine Sub-total G.
29. Line 41: determine the second result by multiplying Sub-total G by the ratio of Sub-total D to Sub-total C, (of if that fraction is less than one half, by one half; or if the fraction is more than one, by one).
30. Line 44: The minimum guarantee fund is calculated by reference to the classes of business for which the company is authorised translated to sterling.

The Minimum Guarantee Fund

- 30A. The amount of the minimum guarantee fund (line 44 of CAP 3) is calculated by reference to the classes of business for which the company is authorised. See Schedule 4 to the Solvency Margin Regulations.

Supplementary Notes

31. Two supplementary notes are required -
 - (i) [Code 0201] – If any of the brought forward amounts differ from the corresponding carried forward amounts in the previous return, the reason should be stated.
 - (ii) [Code 0202] – If any of the amounts included in either CAP 2 or CAP 3 differ from the corresponding amounts in CAP 12 to CAP 15, the amount of difference and the reason for it should be stated.

CAP 4 – Analysis of admissible assets

Valuation and Admissibility of Assets

32. A summary of the valuation rules for assets to be included at each line of CAP 4 and a note of any admissibility restrictions is set out below. Reference in the table to legislation relates to the "Asset Valuation Regulations".

| Line No. | Description | Valuation | Permitted asset exposure |
|----------|--------------------|--|---|
| 11 | Land and buildings | The value will be "not greater than" the amount which (after deduction of the reasonable expenses of sale) would be realised if the land were sold at a price equal to the most recent proper valuation of | 5% of general business amount (GBA) for any single piece of land. Note that, where there is an aggregate valuation, individual parcels of land must be looked at in total and not as individual |



| Line No. | Description | Valuation | Permitted asset exposure |
|----------|---|---|---|
| | | <p>that land (regulation 4). The valuation must be made by a qualified valuer. A qualified valuer is generally a person who has a prescribed professional qualification and who has knowledge or experience in valuing the type of land in question; specific details of the qualifications required are set out in regulation 2(1).</p> <p>The valuation should be based on the consideration received on the open market free of any encumbrance, mortgage or charge, after deduction of expenses of sale. The valuation of buildings should be based on vacant possession and consequently the company may need to consider relocation costs if the building is self-occupied. If there has been no valuation in the last three years the valuation is reported on the form as nil (regulation 4). The "not greater than" rule applies where there have been adverse changes since the previous valuation.</p> | pieces of land (Schedule 1, Part II, para 1). |
| 21&22 | Investments in dependants – shares, debt securities issued by and loans to dependants | Normally a surplus assets basis (regulations 12 and 13). | None directly, (regulation 15(5)(f)), although the dependant's exposure to an asset or to a counterparty will be aggregated with the insurers for the purpose of comparing the business amount. |
| 23 | Other group undertakings and participating interests - shares | Normally a surplus asset basis (regulation 12). | As per rules for non-group shares (lines 41 & 42). A group company that is not a dependant is treated no differently from an unconnected company. |



| Line No. | Description | Valuation | Permitted asset exposure |
|----------|---|--|--|
| 24 | Other group undertakings and participating interests – debt securities issued by and loans to, group undertakings | Amount expected to be recovered, taking into account only the assets identified under regulation 12(2)(a) and any security held in respect of the debt (regulation 13). | As per the rules for non-group securities and loans. |
| 25 | Other group undertakings and participating interests – participating interests | Normally a surplus asset basis (regulation 12). | As for line 27. |
| 26 | Other group undertakings and participating interests – debt securities issued by, and loans to, undertakings in which the insurer has a participating interest. | Amount expected to be recovered, taking into account only the assets identified under regulation 12(2)(a) and any security held in respect of the debt (regulation 13). | As for line 28. |
| 41 | Equity shares, other shares and variable yield securities. | Valued at the middle market quotation for readily realisable shares (see regulation 6(4)), otherwise at assignment value. Special rules apply for securities which are not transferable. | <p>Listed securities:</p> <p>Individual security together with connected companies limited to 2.5% of GBA. 5% restriction in total of listed shares and all other securities in any one company and any of its connected companies (other than for approved counterparties).</p> <p>Unlisted securities:</p> <p>1% of GBA for unlisted shares and all investments (other than secured debt securities or listed investments which are readily realisable) issued by any one company and any of its connected companies. Aggregate limit of 10% of GBA for all such unlisted investments.</p> |
| 42 | Holdings in collective investment | Regulation 10 sets out the characteristics of these collective investment | No restriction where the unit trust falls within the scope of the EC UCIT's |



| Line No. | Description | Valuation | Permitted asset exposure |
|----------|--|--|---|
| | schemes (e.g. unit trusts) | <p>schemes which can be ascribed a value:</p> <ul style="list-style-type: none"> where the issuer can be required to purchase the units or shares, valued at the price that the issuer would have purchased the units or shares (bid price) (regulation 10(2)(a)), and where the issuer cannot be required to purchase the units or shares, valued as for line 41 above (regulation 10(2)(b)). | <p>directive (regulation 15(5)(9));</p> <p>5% of GBA for other authorised/recognised schemes;</p> <p>1% of GBA for unauthorised schemes falling within regulation 10(1)(c).</p> |
| 43 | Approved debt securities and approved other fixed income securities. | <p>These are principally securities, issued by, or guaranteed by, any Zone A government or public authority (regulation 2(1)), and are valued at the middle market quotation in the case of listed securities, at redemption value if not transferable, and in other cases generally immediate transfer value. (regulation 6).</p> | <p>No restriction. Exempt under regulation 15(5)(a).</p> |
| 44 | Other debt securities and other fixed income securities. | <p>If listed, valued at the middle market quotation (regulation 6), but note the definition of listed in regulation 2(1):</p> <p>“there has been granted and not withdrawn a listing in respect of that investment on any stock exchange in an EEA State ... or facilities for dealing in that investment have been granted on a regulated market.”</p> <p>Unlisted debt and other fixed income securities should, where transferable and readily realisable, be valued at market value. Investments which are</p> | <p>Listed securities:</p> <p>5% of GBA. In determining the admissible amount, the aggregate counterparty exposure limits of 5% or 10% must be considered.</p> <p>If the investments are secured, then they follow the admissibility rules for secured debts; i.e. 5% or 10% of GBA being part of the overall counterparty exposure limit.</p> <p>If unsecured, then the limit will vary from 1% to 5% to 10% depending upon the status of the issuer.</p> <p>If the debt is subordinated,</p> |



| Line No. | Description | Valuation | Permitted asset exposure |
|----------|--|--|---|
| | | <p>transferable and not readily realisable are valued at the lower of market value and immediate transfer value, and those which are not transferable are valued at either redemption value or immediate transfer value. (regulation 6(3) and (4)).</p> | <p>then there is a limit of 1% of GBA for unlisted shares and unlisted subordinated debt due from any one company and any of its connected companies.</p> <p>There is also an aggregate limit of 10% of GBA for unlisted shares and unlisted subordinated debt due from any one company and any of its connected companies.</p> |
| 45 | <p>Loans secured by mortgages</p> <p>Note: "secured" in this context has the same meaning as in the Accounts Directive Regulations i.e. the common parlance meaning, which is different from that in the Regulations. Therefore, the assets reported at this line will consist of secured and unsecured loans.</p> | <p>The valuation rules are broadly the same for both secured and unsecured debt, although for secured debts the valuation rules allow due account to be taken of the nature and quality of the security. Both secured and unsecured debts are valued at the amount which can reasonably be expected to be recovered if due within 12 months, otherwise immediate assignment value. (regulation 7).</p> | <p>For secured loans, for each individual 1% of GBA if it is that individual's main residence, otherwise ¼%; for companies 5% of the GBA (in conjunction with all other debts except debts securities). The overall counterparty exposure limits of 5% and 10% of the GBA apply.</p> <p>For unsecured loans, admissibility is considered depending on status of issuer (see Note below). (regulation 15(5)(a)).</p> |
| 46 | Other loans | <p>Investments in limited partnerships may include loans under regulation 6. If this is the case apply the valuation rules for unlisted investments except where non transferable when valued at redemption or surrender value.</p> <p>Other loans, which are not investments, should be valued as debts at immediate transfer value. (regulation 7).</p> | <p>¼% if debt, 1% if investment for each individual amount. 1% for each unincorporated body or company and overall aggregate of 5% for all unsecured debts from individuals and non regulated counterparties.</p> |
| 47 | Deposits with approved credit institutions and approved financial | <p>Amounts generally valued at immediate transfer value. (regulation 7). Deposits with approved</p> | <p>No restriction for approved securities. Deposits with approved credit institutions restricted to</p> |



| Line No. | Description | Valuation | Permitted asset exposure |
|----------|--|--|---|
| | institutions | credit institutions include building society deposits. | 20% of GBA (when deposits are classified as "short term deposits") when combined with all other counterparty exposure to that credit institution and any of its connected companies. There is a more restrictive limit of 10% of GBA applying to all debts other than short term deposits. |
| 51 | Deposits with ceding undertaking. | The amount which can reasonably be expected to be recovered (regulation 7(5)). | No restriction. Exempt under regulation 15(5)(c). |
| 61 to 64 | Reinsurers' share of technical provisions | Valued in accordance with generally accepted accounting principles. (regulation 7). | No restriction. Exempt under regulation 15(5)(c). |
| 71 | Debtors arising out of direct insurance operations | The amount which can reasonably be recovered. As for other debtors, the normal valuation rules and principles relating to debts apply. (regulation 7(7) but see timing restriction below). Any prepared commission to an intermediary is to be valued at nil (regulation 7(6)). Any premium debts which are recorded in the accounting records as due and payable and which have been outstanding for more than three months are inadmissible. This applies to all premium debts, including debts due in relation to reinsurance business accepted. It does not apply to debts due in relation to reinsurance contracts ceded. The timing for the three months test is important: for instalment premiums this will start from the | No restriction. Exempt under regulation 15(5)(c). |



| Line No. | Description | Valuation | Permitted asset exposure |
|----------|---|--|--|
| | | date each particular instalment is due. | |
| 72 | Salvage and subrogation recoveries | The value of any salvage or subrogation rights shall be the amount which can reasonably be expected to be recovered if the right(s) is(are) exercised. (regulation 7(8)&(9).) | No restriction. Exempt under regulation 15(5)(c). |
| 73 | Debtors arising out of reinsurance operations, due from ceding insurers and intermediaries under reinsurance business accepted. | Same as for 71 above. | Same as for 71 above. |
| 74 | Debtors arising out of reinsurance operations, due from reinsurers and intermediaries under reinsurance contracts ceded. | The amount that can reasonably be expected to be recovered. (regulation 7(5)). | No restriction. Exempt under regulation 15(5)(c). |
| 75 | Other debtors - due from dependants | Dependants rules apply – “look through” to the underlying asset. (regulations 12 and 13 and regulation 6) | No restriction. Exempt under regulation 15(5)(f). |
| 76 | Other debtors - other | The valuation rules are broadly the same for both secured and unsecured debt, (for secured debts, the valuation rule allows due account to be taken of the nature and quality of the security). Both secured and unsecured debts are valued at the amount which can reasonably be expected to be recovered if due within 12 months, and if due in more than 12 months at immediate assignment value, i.e. will reflect time value of money for period of the debt. (regulation 7(1) and (4)). | For secured debts, the overall counterparty exposure limits of 5% and 10% of the GBA apply. For unsecured debts, admissibility is graded depending on status of issuer (see Note 1 below). |



| Line No. | Description | Valuation | Permitted asset exposure |
|----------|--|---|---|
| 81 | Tangible assets | <p>All equipment owned by the company (excl. computer software) is valued as below.</p> <p>Computer equipment</p> <p>(a) In the financial year of purchase the amount is limited to 75% of the cost.</p> <p>(b) In the next financial year the amount is limited to 50% of the cost.</p> <p>(c) In the third financial year the amount is limited to 25% of the cost.</p> <p>(d) In subsequent years the computer is valued at nil.</p> <p>The "not greater than" rule applies.</p> <p>Other equipment</p> <p>In the financial year of purchase the amount is limited to 50% of the cost, but nil in the years after the year of purchase. The "not greater than" rule applies.</p> | <p>5% of GBA.</p> <p>2.5% of GBA.</p> |
| 82 | Cash at Bank: Deposits not subject to time restriction or withdrawal, with approved credit institutions and approved financial institutions and local authorities. | As 47. | <p>As 47 in respect of deposits with approved credit institutions. If banks are not approved credit institutions then admissibility is restricted to 1% of GBA.</p> <p>If deposits with approved financial institutions or with local authorities (assuming they are within Zone A), no restrictions (regulation 15(5)(a)).</p> |
| 83 | Cash in hand | Face value (note: this refers to actual cash, not deposits which must be valued as referred to above). | 3% of GBA. (Schedule 1, Part II, para 18). |
| 84 | Other assets. | Value will depend upon the asset in question. In view of the requirement | Admissibility will depend upon the asset in question. |



| Line No. | Description | Valuation | Permitted asset exposure |
|----------|--|---|--|
| | | of regulation 3(3) to leave out of account assets for the valuation of which no specific provision is made, it will be rare to have entries at this line and a supplementary note is required to give particulars. | |
| 85 | Accrued interest and rent | Debts (regulation 7). | None for interest on approved securities (regulation 15(5)(a)). Otherwise as for debts (see lines 76 to 79). |
| 86 | Deferred acquisition costs | Valued in accordance with generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate for insurers. | None. Regulation 15(5)(h). |
| 87 | Other prepayments and accrued income | Debts (regulation 7), if an amount could be collected, otherwise inadmissible. | Debts (see lines 76 to 79). ¼% of GBA due from an individual, 1% from a corporate body and subject to aggregate limit of 5% (Schedule 1, Part II). |
| 88 | Deductions (under regulation 15(2)(b) and 15(3) of the Regulations) from the aggregate value of assets | This item relates to the deduction from total admissible assets which may be necessary where the company does not have sufficient assets of that description to eliminate the excess of the permitted assets exposure limit for such assets. If it is not intended that this line is used for specific inadmissible assets, then only the admissible element is included in the appropriate line with the inadmissible element in line 92. (regulation 15). | n/a. |

Note: For unsecured debts, admissibility will depend upon who the debt is from. These are as follows:

- approved counterparties – part of the overall counterparty exposure limits of 10% of GBA.



- Regulated institutions – 2.5% of GBA for any one institution (and connected companies);
- Other corporate bodies – 1% of GBA for a single debt and 5% in aggregate for all unsecured debts due from such bodies and debts due from individuals; and
- Individuals – 0.25% of GBA for any single debts and 5% in aggregate as described above.

Where an asset has to be left out of account because it is not specifically referred to in the Regulations, the Commissioner is generally prepared to discuss the matter with the company and its advisers, and may (but will not create a precedent by doing) issue a Section 113 concession order allowing the company to bring the asset into account on an agreed basis of valuation.

Completion of the Form

33. The form consists of 3 parts.
- Lines 11 to 89 provide a “line by line” analysis of the assets valued in accordance with regulation 4 of the Regulations. The classification used follows, as near as possible, the balance sheet headings used for the statutory accounts.
 - Lines 91 to 99 provide a reconciliation between the total assets as valued in accordance with regulation 4 and as valued in accordance with the Insurance Companies (Accounts Directive) Regulations 1997 (the “Accounts Directive Regulations”).
 - Line 100 discloses the value of the debts due from related companies, other than those under contracts of insurance or reinsurance.
34. Regulation 4 provides that assets are to be valued in accordance with Part II of the Asset Valuation Regulations.
35. Lines 11 to 87 show asset values after deduction for excess over permitted asset exposure limits – see regulation 15 of the Asset Valuation Regulations. Where such a deduction relates to assets included at more than one line of CAP 4, it should be apportioned pro-rata. Negative amounts should not be shown at lines 11 to 87. If a deduction is more than the value of the assets to which it relates the ‘excess’ element of the deduction should be shown at line 88, as also should deductions for excesses over permitted counterparty limits and for excess concentrations over a number of counterparties.
36. The value of any asset denominated in a currency other than sterling be converted into sterling using the year end closing middle rate – paragraph 3 of Schedule 1. (But see para. 6 of this Guidance Note).
37. The amount of any asset in CAP 4 should be shown gross of any set-off against any corresponding liability (which liability should be shown on CAP 5). The only exception to this is where –
- amounts are owed from and to the same person, and
 - such netting is permitted under generally accepted accounting principles.
- 37A. The above rule usually prevents the set-off of amounts due from and to the same broker/intermediary unless they relate to the same client of the broker. This is because, typically, such amounts are, in law, owed from and to the client and not the broker/intermediary. The broker/intermediary merely acts as a collecting agent.

- 37B. Line 47 "Deposits with approved credit institutions and approved financial institutions" should only show relevant deposits subject to a time restriction on withdrawal. Deposits not subject to such a time restriction should be shown at line 82.
- 37C. The amount at line 61 will need to be adjusted to remove any discount to take account of investment income where this adjustment has been made to the gross provision (see instruction 13 to Form INS 5 and paragraph 47).
- 37D. Line 73 "salvage and subrogation recoveries" should only be used for such recoveries which fall to be classified as "debtors arising from insurance operations". Occasionally some salvage or subrogation recoveries may be classified under other headings in the statutory accounts in which case the same heading should be used in CAP 4, but a supplementary note [code 0503] is required. If salvage and subrogation recoveries are shown in the statutory accounts as a deduction from liabilities rather than as an asset, the same treatment should be adopted in the Annual Returns. i.e. line 73 should be left blank and the amount of liabilities shown on CAP 5 shown net of the salvage and subrogation recoveries.
- 37E. Line 80 should include leased tangible assets where such are held under a finance lease and are brought into account as an asset in the statutory accounts in accordance with Statement of Standard Accounting Practice 21.
- 37F. Line 84 "Other Assets" refers to the balance sheet heading in the statutory accounts of "Other Assets – other" (item Fv in the balance sheet format in Schedule 1 to the Accounts Directive Regulations). It should not be used for any other type of asset and, even where used for an asset falling under the statutory accounts Fv heading, it should show only the admissible value, if any.
38. Lines 91 to 99 reconcile the admissible assets to the total assets determined in accordance with the statutory accounts rules. This reconciliation must be completed. A particular problem is caused by those assets which the Accounts Directive Regulations permit to be shown either as assets or as a deduction from liabilities. The main classes of such assets are-
- the reinsurers' share of technical provisions, and
 - the deferred acquisition costs.
39. These assets, to the extent admissible, should always be shown at line 61 to 64 and 86 respectively. Further, the total shown at line 99 ("Total assets determined in accordance with the Accounts Directive Regulations") should always include such assets even where they are actually shown as a deduction from liabilities in the statutory accounts.
40. Apart from the above, the Commissioner does not believe that there is any other reason why an item should not be classified as an asset or a deduction from liabilities on CAP 4 (line 99) and CAP 5 in the same way as in the statutory accounts. The same applies for the classification of an item as a liability or a deduction from assets. Different methods of 'grossing up' should be avoided.
41. The statutory accounts rules allow for some investments to be valued either at current value or at amortised cost. An insurer should choose the same method for line 99 on CAP 4 as it chooses for its statutory accounts.
42. Asset valuation differences arising in respect of shares in, or debts due from, or to become due from, dependants should be included:
- (i) at line 92, in so far as they arise from the application of admissibility limits to the assets of that dependant;

- (ii) at line 93, in so far as they arise from a solvency margin deduction made either because that dependant is itself an insurer or because it (directly or indirectly) has invested in another dependant which is an insurer; and
- (iii) at line 94, in respect of any other causes of differences.

Line 95 should not be used for differences arising in respect of shares in, or debts due from, or to become due from, dependants. Such shares or debts are not themselves "assets of a type not valued", and this is still true even if the dependants themselves invest in assets of a type not valued.

Supplementary Notes

43. Nine supplementary notes are required -

- (i) [Code 0401] – The aggregate value of (i) unlisted investments, (ii) certain listed investments, (iii) units or beneficial interest in certain collective investment schemes and (iv) reversionary interests or remainders in property other than land or buildings, together with a description of the assets in question [items included in lines 41 to 44].
e.g. A single figure with a simple description will suffice. For example: The company held £xm in unlisted securities and £ym in unregulated collective investment schemes, almost all of which were of the latter type. The assets covered by this note are those which count towards the 10% permitted asset exposure limit at paragraph 13 of Part II of Schedule 1 to the Asset Valuation Regulations. For detailed definitions of the type of assets to be included, see Part II of those Regulations.
- (ii) [Code 0402] – the aggregate value of hybrid securities included in lines 43 and 44.
- (iii) [Code 0403] – the amounts of any non-debtor salvage or subrogation recoveries included other than at line 72.
- (iv) [Code 0404] – a statement that amounts have been set-off to the extent permitted by generally accepted accounting principles (if this option has been exercised) – see paragraph 7 of Schedule 1.
- (v) [Code 0405] – the maximum counterparty limit permitted by the company's investment guidelines (and any separate limit for counterparties other than "approved counterparties") together with an account for any breaches during the year of those limits – see paragraph 10(1) of Schedule 1:

The precise content of this "account" of any breach is not specified in the Regulations. However, the Commissioner expects it typically at least to include an estimate of the amount of the excess and the reasons why it was permitted to arise. [The requirement to give an account of any breaches during the year should not be read as implying that real-time monitoring of the exposures is necessary. Rather, the frequency of the monitoring should be appropriate to the make-up of the investment portfolio].

For the purpose of making the disclosures required by supplementary notes 0405 and 0406, "counterparty" has the same meaning as in paragraph 1 of Part I of Schedule 1 to the Asset Valuation Regulations. Also, the amount of any counterparty exposure should be calculated using the rules laid down in paragraphs 13 to 15 of Part II of the Schedule, except that asset values should not be limited to the amounts of any permitted asset limits. The amount of any counterparty

exposure should be stated before deduction of any excess counterparty exposure or excess concentration with a number of counterparties.

Assets excluded from the scope of the counterparty exposure rules may also be disregarded for the purposes of disclosure in these supplementary notes. This excludes assets of the type listed in regulation 15(5). [For a list of such asset types see paragraph 131 of Guidance Note No. 4 on the Valuation of Assets].

- (vi) [Code 0406] – the amount and nature of the exposure at the year end to large counterparties (i.e. greater than 5% of the GBA) – see paragraph 10(2) of Schedule 1.
- (vii) [Code 0407] – the aggregate value of certain fully secured rights – see paragraph 10(3) of Schedule 1.

This disclosure covers those secured assets which are exempted from counting towards the appropriate permitted counterparty exposure limit by virtue of paragraph 14 of Part I of Schedule 1 to the Asset Valuation Regulations. (N.B. By no means are all secured assets so exempted). Secured assets which are exempted from the limit by virtue of some other provision should not be included. A single aggregate figure is sufficient disclosure.

- (viii) [Code 0408] – the amount of any tangible leased assets included at line 81.
- (ix) [Code 0409] – particulars of any “Other assets” included at line 84.

CAP 5 – Liabilities

Completion of the Form

44. The form consists of 3 parts
- Lines 11 to 59 provide a “line by line” as far as possible, analysis of the liabilities (other than share capital and reserves) corresponding to the balance sheet headings used in the statutory accounts.
 - Lines 62 and 63 list two further items of liability – (i) cumulative preference share capital and (ii) subordinated loan capital.
 - Line 71 discloses the value (as included in the above items) of the liabilities to related companies, other than those under contracts of insurance or reinsurance.
45. Amounts in lines 11 to 13 and 16 will be stated gross of reinsurer’s share.

Determination of Liabilities

Lines 11 to 19

46. The liabilities at lines 11 to 59 should be valued in accordance with Part III of the Asset Valuation Regulations, the main provision of which is regulation 18 which provides that –
- “(1)... the amount of liabilities of an insurer shall be determined in accordance with generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate for insurers”.
- “(2)In determining under sub-regulation (1) the amount of liabilities of an insurer, all contingent and prospective liabilities shall be taken into account including all liabilities in respect of cumulative preference share capital but excluding other liabilities in respect of share capital.”

47. The sub-regulation (1) requirement that generally accepted accounting concepts etc. be used means, in effect, that the liabilities at lines 11 to 59 are to be valued for the return in the same way as for the statutory accounts, except in relation to the technical provisions for claims outstanding. For technical provisions, this is indeed explicitly stated by regulation 19A of the Asset Valuation Regulations which refers to the rules in Section D of Chapter II of Schedule 1 to the Accounts Directive Regulations. Regulation 4(7) of the Solvency Margin Regulations, however, requires that (with certain exceptions), the margin of solvency be reduced by the difference between the discounted (to take account of investment income) and undiscounted technical provision for claims outstanding. Instructions 3 to INS 7 (and instruction 13 to form INS 5) therefore requires the amounts at line 12 of Form INS 7 and line 61 of Form INS 5 to be increased to show amounts that are undiscounted. The adjustment is not required for pure reinsurers which do not have authorisation to effect contract of insurance, nor is it required in relation to annuities or class 1 or 2 business.
48. Sub-regulation (2) does not require that the “amount” of every prospective and contingent liability be set equal to the full extent of its nominal value regardless of the remoteness of the contingency it represents. The requirement is merely that all prospective and contingent liabilities “be taken into account”, i.e. considered. The amount of every liability, whether present, prospective or contingent, should be set as required by sub-regulation (1) in accordance with generally accepted accounting concepts etc.
49. The above does not mean that the value shown for such liabilities in the return will always necessarily be the same as that shown in the statutory accounts. Exceptionally, differences may occur if the return and statutory accounts are signed off at different dates. In such a case, it is possible that a material adjusting post-balance sheet event may have occurred between the date of the sign off of the statutory accounts and the date of the sign off of the return (or vice versa).

Lines 62 and 63

50. Share capital is not normally to be considered a liability for the purposes of completing the return – see regulation 18(2) of the Asset Valuation Regulations. The only exception (see regulation 4(2)(e) of the Solvency Margin Regulations) is cumulative preference share capital, but this exception is, in turn, subject to a partial exemption as explained below.
51. In determining whether an insurer has assets in excess of its liabilities, the full nominal value (plus any premium on redemption, if redeemable) of all cumulative preference share capital is to be counted as a liability. If the assets exceed liabilities, then part (sometimes all) of the liability from the preference share capital may be disregarded in determining whether the net assets exceed the required margin of solvency.
52. In line 62, the full value of cumulative preference share capital is to be shown, i.e. the value to be used in determining whether the insurer has assets in excess of liabilities. This full value then forms part of the total liabilities which are taken from CAP 5 to CAP 1 where they are compared with the total assets taken from CAP 4. If assets exceed liabilities, the part of the liability for preference share capital which may be disregarded in determining whether the net assets exceed the required margin of solvency, is added back as an adjustment to net assets on CAP 1. No adjustment is to be made on CAP 5.
53. Subordinated loan capital is to be valued according to the basic rule in regulation 18, i.e. in accordance with generally accepted accounting concepts etc.. Where an insurer has been granted a section 113 Order permitting it to

disregard all or part of the liability for its subordinated loan capital in determining whether its net assets exceed its required minimum margin, the adjustment for the amount to be disregarded is to be made solely on CAP 1 and not on CAP 5. (The reason for this treatment of the add-back is the same as that described above for the add-back in respect of preference share capital).

Supplementary notes

54. Four supplementary notes are required -
- (i) [Code 0501] – Specified details should be stated of (a) any charges over assets, (b) potential capital gains tax liability (if applicable), (c) contingent liabilities, (d) guarantees, indemnities or other contractual commitments, effected other than in the ordinary course of insurance business, in respect of related companies, and (e) any other fundamental uncertainty – see paragraph 12(1) of Schedule 1. [Refer to paragraph 123 of Guidance Note No 2A on the preparation of Annual Returns for general business insurers and reinsurers.]
 - (ii) [Code 0502] – The aggregate amount of any accrued dividend on any cumulative preference share capital issued by the insurer should be stated.
 - (iii) [Code 0503] – The amount of each provision made under regulation 19B of the Insurance Companies (Valuation of Assets and Liabilities) Regulations 1996 in respect of a deficit in a related undertaking which is an insurance undertaking or insurance holding company and the identity of the undertaking should be stated. Such provision should be included in line 22 of CAP 5.
 - (iv) [Code 0504] – Where technical provision for claims outstanding have to be increased in accordance with instruction 3 to form INS 7 to remove discounting, the amount of the increase, together with the corresponding increase in the reinsurer’s share shown in line 61 of CAP 4 must be shown.

CAP 6 – Profit and loss account (non-technical account)

Completion of the Form

55. The headings used on CAP 6, as far as possible, are based on those used in the “Profit and Loss Account – Non Technical Account” format in the statutory accounts and, except where referenced to other Forms, the amounts included under those headings should be determined using the same rules as apply for the statutory accounts.
56. Unrealised gains and losses on investments should be included in their entirety at lines 15 and 18, even if different accounting treatment is adopted in the statutory accounts. Unrealised gains and losses should be measured by reference to the value included for the investment at line 99 on CAP 4. An insurer which includes investments at amortised cost at line 99 on CAP 4 should show the unrealised gain and loss relative to the amortised cost, not to current market value.

Supplementary Notes

57. Four supplementary notes are required -
- (i) [Code 0601] – The bases of conversion adopted in respect of foreign currency for income and expenditure should be stated – see paragraph 4(2) of Schedule 1.

- (ii) [Code 0602] – In addition to the above, the Commissioner requests that, where any brought forward amounts on any Form are restated due to currency reconversion, this fact be briefly stated in a supplementary note to CAP 6. A simple statement of this fact is all that is needed, e.g. “Some of the brought forward amounts shown in the Forms [xx to xx] have been restated from the corresponding carried forward amounts included in the previous years’ return due to the reconversion of foreign currency amounts at a different rate of exchange.” No further details need be given.
- (iii) [Code 0603] – Particulars of any amounts included at line 16 or 21 on CAP 6 should be stated.
- (iv) [Code 0604] – Particulars of any amounts included at line 41 on CAP 6 should be stated.

Accident Year And Underwriting Year Accounting

The basic rule

58. The basic rule is that an insurer may choose whether to account for its business on an accident year basis or an underwriting year basis. This choice may be made separately for each accounting class and, indeed, separately for any clearly definable part of an accounting class.
59. Where risks are accounted for on an accident year or underwriting year basis, the run-off of those risks must continue to be accounted for on the same basis. The insurer remains free, however, to account for the renewals of such business on either basis.
60. Under the new Regulations there is no longer a direct link between the basis of reporting (i.e. underwriting year or accident year) and the method of profit recognition (i.e. annual or non-annual). An insurer may change its basis of profit recognition, even for risks previously reported, from non-annual to annual. However, even where it makes such a change, it must continue to report the run-off of such risks on an underwriting year basis.

Accounting for premiums, claims and expenses

The accounting rules

61. The amounts shown in the return for –
- “gross premiums written”, “reinsurers’ share”, “earned premiums” etc.;
 - “claims outstanding”, “claims incurred”, “gross amount”, “reinsurers’ share” etc;
 - “provision for unearned premiums”, “provision for unexpired risks”, “deferred acquisition costs”; and
 - “net operating expenses”, “acquisition costs”, “administrative expenses” and “reinsurance commissions and profit participations”
- should be determined –
- using the same rules as apply for the preparation of the statutory accounts (see regulation 3(2)(b) which aligns definitions with those in “the Accounts Directive Regulations”; and
 - in accordance with generally accepted accounting practice (paragraph 25(1) of Schedule 2).
62. In particular, contracts of financial (re)insurance whether inward or outward should be classified for inclusion in the forms in accordance with FRS 5

“Reporting the substance of transactions” and the statement “FRAG 35/94: The Application of FRS 5 to Non-Life Insurance Transactions.” Thus, where the consideration receivable and payable for transactions which have the legal form of contracts of insurance or reinsurance would not be accounted for as premiums and claims in the preparation of statutory accounts, they should not be included as premiums and claims in CAP 10 to CAP 15. Instead, they should be accounted for in the return using the same principles as are applied in the preparation of the statutory accounts.

63. An exception to the rule in paragraph 61 above (i.e. the alignment of definitions with those in the Accounts Directive Regulations) is that claims amounts shown in the forms should exclude –
- claims management costs, and
 - adjustments for discounting.
- Some forms exclude these items altogether and other forms provide for their separate disclosure. [See paragraph 14 to Schedule 2]
64. Another exception is that the rules for the statutory accounts analyse “net operating expenses” into (i) “acquisition costs”, (ii) “administrative expenses” and (iii) “reinsurers’ commissions and profit participations” whereas the forms sub-analyse the first item into “commissions” and “other acquisition expenses”.
65. Claims management costs are basically those costs which are required to be included in the amount for incurred claims shown in the statutory accounts. (See regulation 3 for the exact definition.)
66. In Forms CAP 10 to CAP 15, (as in the technical account in the statutory accounts), claims incurred include any reduction for salvage and subrogation recoveries.
67. Paragraphs 8 to 13 of Schedule 2 lay down rules as to how premiums and claims are to be allocated to accident years and underwriting years. It needs to be noted here that the paragraphs do not define premiums and claims. They assume the definition given elsewhere in the Regulations (see paragraph 61 above) and merely address the question of allocation.

Accident year accounting

68. For accident year accounting, premium is allocated to accident years on the basis of when it is earned, and claims are allocated on the basis of when the incident occurred which gives rise to the claim. Special rules apply for (i) claims-made policies and (ii) the reinsurance (or a Schedule 10 transfer) of policies covering incidents which had already occurred at the time of the reinsurance (or transfer).
69. An incident giving rise to a loss under a claims-made policy is deemed to occur on the earlier of date of notification or the last date of the period for which cover is provided. The latter of the two alternative dates would usually only be relevant if the claims-made policy is not renewed and if upon non-renewal, the policy allows a “sunset” period, (i.e. a period during which claims relating to events which took place prior to the end of the cover period may still be notified).
70. Where an insurer reinsures, (or receives by way of a Schedule 10 transfer), policies covering incidents which had already occurred prior to the date of the contract of reinsurance (or of the transfer), all such incidents are deemed to occur at the date of the reinsurance contract (or of the transfer).
71. Net operating expenses should be allocated to accident years so as to match them to the related premium earned and claims incurred. Usually, this will

result in the bulk of administrative expenses being allocated to the youngest accident year. [Note that administrative expenses do not include claims management costs.]

Underwriting year accounting

72. For underwriting year accounting, premiums and claims are allocated to underwriting years on the basis of when policies incept. For these purposes –
- a policy providing continuous cover is deemed to incept on each anniversary of the policy; and
 - policies received by way of a Schedule 10 transfer (or equivalent transfer under the law of an EEA State) are deemed to incept on the date of the transfer.
73. Net operating expenses should be allocated to underwriting years so as to match them to the related premium earned and claims incurred. Usually, this will result in the administrative expenses being allocated to the youngest underwriting year except to the extent that it represents the adjustment for under- or over-provisions of such expenses in the prior years. [Note that administrative expenses do not include claims management costs.]

The annual and non-annual methods

74. The annual and non-annual methods refer to the way in which profit is recognised. Under the annual method, the profit (and losses) on business written during the financial year is recognised at the end of that financial year by setting up provisions for outstanding claims, unearned premiums and unexpired risk reserves and by deferring an appropriate portion of acquisition costs.
75. Under the non-annual method (i.e. fund accounting), the recognition of profits (but not losses) is deferred for one, two or three years after the end of the financial year in which business incepts. During the period of the deferral, the technical provision for such business is the excess of premiums written over claims and expenses (increased where necessary to the extent of any losses expected to arise on such business). At the end of the deferral period, this original technical provision is replaced by a technical provision determined under the same rules as apply for the annual method, (i.e. a technical provision which consists of provisions for outstanding claims, unearned premiums and unexpired risk reserves), and by the deferral of an appropriate portion of acquisition costs. The choice of the deferral period should usually be consistent from year to year, but may differ from one type of business to another.
76. The detailed rules for the non-annual method are to be found in paragraphs 51 and 52 of Schedule 1 to the Accounts Directive Regulations. [Note: Schedule 1, as such, strictly only applies to the preparation of statutory accounts. However, regulation 19A of the Asset Valuation Regulations requires that the Schedule 1 rules on the valuation of general business liabilities also be followed for our solvency purposes.] Also of relevance is the ABI SORP (published in December 1998) in so far as it is a statement of “generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate for insurers”. [See regulation 18 of the Asset Valuation Regulations which requires such generally accepted concepts etc. to be followed for our solvency purposes.] It is recommended that insurers obtain a copy of the ABI SORP.

The relationship between the reporting basis and method of profit recognition

77. In the Returns prepared under the 1996 Regulations, there was a strict relationship between the reporting basis (i.e. accident year or underwriting year) and the method of profit recognition (i.e. annual method or non-annual method). This is no longer the case under the new Regulations.
78. An insurer which wishes to apply the annual method may report that business on either the accident year forms or the underwriting year forms. However, if it wishes to apply the non-annual method, it must report such business on the underwriting year forms. This relationship is summarised by the table below:

| Reporting basis | Profit recognition method |
|-------------------------|------------------------------------|
| Underwriting year basis | Annual method or Non-annual method |
| Accident year basis | Annual method |

The non-annual method – “closed” and “open” years

79. Business to which the non-annual method of profit recognition is applied is classified into “open” and “closed” underwriting years.
80. As already described above, under the non-annual basis, a technical provision is originally set up as the excess of premiums written over claims paid and expenses (increased where necessary to the extent of any losses expected to arise on such business). At the end of the deferral period, the original technical provision is replaced by one determined on the same basis as applies under the annual method. An underwriting year is termed “closed” with respect to any business if the replacement of the original technical provision has been made in respect of that business, otherwise it is termed “open”.
81. Significantly less disclosure is required on the underwriting year forms for “open” years than for “closed” years. Business reported on the underwriting year forms but to which the annual method has been applied are subject to the same level of disclosure on those forms as applies for “closed” years business.
82. The technical provision for an open year for an accounting class is the fund represented by –
- premiums written (net) - claims paid (net) - expenses incurred**
83. Any excess, over the fund, of present and future liabilities from business incepting in that year falling in that accounting class is termed a “deficit”. Any excess of the fund, for the present and future liabilities from business incepting in that year falling in that accounting class, is termed a “surplus”.
84. A deficit on any open year for any accounting class must be dealt with by either-
- offsetting the deficit against surpluses (in the same year) arising on business falling in other accounting classes which is “managed together” with the business giving rise to the deficit; and/or
 - increasing the technical provision.
85. Business may only be regarded as “managed together” if it –
- is accounted for on an underwriting year basis;
 - incepts in the same accounting year; and

- may be regarded as “managed together” under generally accepted accounting practice.

[This definition of “managed together” is given in paragraph 24 of Schedule 2.]

Conversion from the non-annual to the annual method

86. An insurer which has previously reported business on a non-annual basis and wishes to convert to an annual basis may do so in one of two ways. It may either –
- continue to report that business (including new business and renewals) on the underwriting year forms but close all underwriting years including the youngest year; or
 - report new business and renewals on the accident year forms, but continue to report old business (i.e. risks incepting prior to the current year) on the underwriting year forms and close all underwriting years on those forms.
87. An insurer may not transfer business previously reported on underwriting year Forms (INS 24) to the accident year Forms (INS 21). [i.e. CAP 14 to CAP 11]. The basic rule is that, when any risks are reported on either underwriting year or accident year forms, the run-off of those risks must continue to be reported to the same forms. However, renewals may be reported on either of the forms.

Supplementary note disclosure

88. Paragraph 23 of Schedule 2 requires that the following be stated by way of supplementary note to Form INS 24 (CAP 14) in respect of each accounting class which (in whole or in part) is reported on the underwriting year forms –
- the reason for accounting for such business on an underwriting year basis;
 - the basis for distinguishing such business and any other business falling within the same accounting class accounted for on an accident year basis; and
 - the accounting policy adopted for determining the provision for claims outstanding (i.e. the annual method or the non-annual method).
89. The above information need only be given in respect of risks incepted during the financial year. However, if the information differs from that which applies for risks of a similar description incepting in the previous financial year, the difference should be described and the reason for it given.
90. If the non-annual method is disclosed as the accounting policy adopted, the following should also be stated in the supplementary note [Code 1402] –
- the reason for using the non-annual method;
 - the basis for distinguishing between such business and other business in the same accounting class reported on the underwriting year forms;
 - the normal period for which an underwriting year is left open, or if that period differs for different types of business within an accounting class –
 - (i) the basis of distinguishing between different types of business, and
 - (ii) the normal period for each type; and

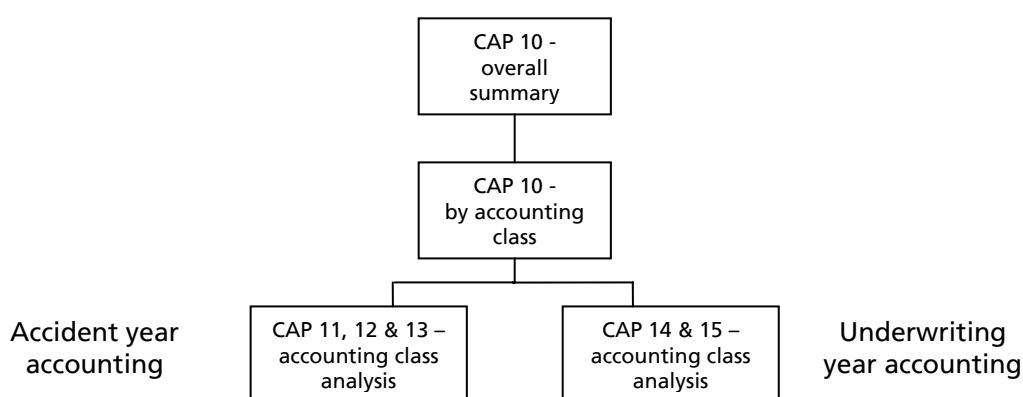


- where an underwriting year is left open for longer than the normal period, the reason for not closing the year.

Accounting Classes, Business Categories And Risk Group

An overview of the Forms

91. There has been a simplification to the normal requirement under the Regulations in that fewer forms will be required. There will be no requirement with these abbreviated returns to provide information either by "risk groups" for direct business and facultative reinsurance business or by "business categories" for treaty business. However, the Schedule 5 information is required by risk groups and business categories.
92. The reporting of business within the abbreviated return is summarised by the following diagram.



Accounting Classes

93. There are eight direct and facultative accounting classes and three treaty classes. These are defined by regulation 3 and paragraph 6 of Schedule 2. The following table summarises the definition.

| | | |
|--|-----------|---|
| Accounting classes for direct insurance and facultative reinsurance | 1 | accident and health |
| | 2 | motor |
| | 3 | aviation |
| | 4 | marine |
| | 5 | transport |
| | 6 | property |
| | 7 | third party liability |
| | 8 | miscellaneous and pecuniary loss |
| Accounting classes for treaty reinsurance | 9 | non-proportional treaty |
| | 10 | proportional treaty |
| | 11 | marine, aviation and transport (MAT) treaty |

94. The accounting classes (other than the special case of accounting class "11" which is explained below) correspond closely to those used in the "1996 Regulations". The only differences are that –



- death or injury to passengers may now be included in either accounting class 1 or split across accounting classes 2, 3 and 4 (see below); and
 - inwards proportional retrocessions of non-proportional treaty reinsurance should be included in accounting class 9.
95. Brought forward amounts should, where necessary, be restated in the first return submitted under the new Regulations to reflect these changes in definitions.
96. There is some flexibility to include the following items in a different accounting class from that which would be required by the above table –
- hovercraft business,
 - liability for loss of, or damage to, goods in transit,
 - death or injury to passengers.
97. Refer to paragraph 6 of Schedule 2 for the detailed rules. A supplementary note to CAP 10 is required if this option is used. It should state the nature of the business included in a different accounting class and the reason for such inclusion. The nature of business included in a different accounting class should be consistent from year to year.
98. Accounting class 11 calls for special comment. The basic rule is that all treaty business should be included as either proportional in accounting class 10, or non-proportional in accounting class 9. No business is thus included in accounting class 11. However, as the Regulations allow an alternative to the basic rule, an insurer may choose to include (some or all) of its MAT treaty business in accounting class 11. If it does so, it must state in a supplementary note the nature of the business so included and the reason for the inclusion. The nature of business included in accounting class 11 should be consistent from year to year.

Forms CAP 10 To CAP 15

CAP 10 – General Business Technical Account

Completion of the Form

99. CAP 10 should be prepared separately for each accounting class (where any business falling in that accounting class has been carried on) and also in summary. The form represents the technical account and consists of 4 parts –
- a technical account for this accident year (lines 11 to 19)
 - a technical account for prior accident years (lines 21 to 29)
 - the balance from underwriting year accounting (lines 31 to 39) and
 - the investment return allocated to the technical account (line 51).
100. The two accident year technical accounts relate only to business accounted for on an accident year basis. CAP 14 presents the technical account for underwriting year business and it is from this that the balance at line 31 derives.
101. The items in the two accident year technical accounts derive from CAP 11 (earned premiums) and CAP 12 (claims, expenses, etc.). The only item which does not derive from other forms is “Other technical income or charges” (lines 16 and 25). If any amount is entered in these lines particulars must be stated in a supplementary note.

102. Line 32 is to accommodate other technical income and charges arising from business accounted for on an underwriting year basis. Such other income and charges should not be included on CAP 14. A supplementary note is needed.
103. The allocated investment income (line 51) is linked to line 20 of CAP 6. The allocation, if any, should be the same as in the statutory accounts.

Supplementary Notes

104. Six supplementary notes are required –
- (i) [Code 1001] – Where an insurer exercises any of the options in paragraph 6 of Schedule 2 to report business in a different accounting class, it should state (a) the nature of the business it has included in that different accounting class and (b) the reason for such inclusion – see paragraph 7 of Schedule 2.
 - (ii) [Code 1002] – For each accounting class, an insurer should state, separately for business accounted for on an accident year basis and on an underwriting year basis, the split of (a) total gross premium written and (b) reinsurers' share of gross premium written between business attributable to Gibraltar and to non-Gibraltar business – see paragraph 15 of Schedule 2. For these purposes, direct and facultative business is Gibraltar business if the contract was made in Gibraltar and treaty reinsurance is Gibraltar business if the cedant has its head office in Gibraltar.
 - (iii) [Code 1003] – If an insurer has effected no new contracts of insurance of any one or more authorisation class during the financial year, it should state the date on which the last new contract of each such class was effected – paragraph 20 of Schedule 2. A "new contract" is any contract other than one effected in fulfilment of an obligation under an already existing contract of insurance.
 - (iv) [Code 1004] – Where "contracts of insurance", both inwards and outwards, have been excluded as a result of following FRS 5 and FRAG 35/94 i.e. they are financial insurance/reinsurance, extensive disclosure is required – see paragraph 25 of Schedule 2.
 - (v) [Code 1005] – Particulars should be stated of any amounts included at lines 16 or 25 (accident year accounting – other technical income or charges) or line 32 (underwriting year accounting – other technical income or charges).
 - (vi) [Code 1006] – Details of any material connected party transaction as required under regulation 18A should be stated (see Annex 4).

CAP 11 – Analysis of premiums – accident year accounting

Completion of the Form

105. CAP 11 should be prepared separately for each accounting class. No summary form is required. The form presents an analysis of premium for business accounted for on an accident year basis. Premiums should be shown gross, i.e., before commissions payable.
106. In lines 11 and 12, premiums notified in the current year which relate to previous years' business should be entered in line 11 if it is fully earned in the previous year, or in line 12 if it is part earned/unearned in the current year.
107. Lines 13 to 15 should include premiums actually received prior to the financial year but relating to risks incepted in the financial year, and exclude premiums received during the financial year but relating to risks incepting after the end



of the financial year. In CAP 4 and CAP 5, the accounting treatment adopted for premiums received in respect of risks incepting in future financial years should be the same as that adopted in the statutory accounts or, if this results in different amounts for the provision for unearned premium (either gross or the reinsurer's share) being shown in CAP 4 or CAP 5 as compared to CAP 11, the Commissioner requests that the difference be identified and explained in a supplementary note [Code 1103].

108. Line 16 shows premiums receivable in previous financial years not earned in those years and brought forward to the current financial year (i.e. unearned premium provision brought forward).

Supplementary Notes

109. Three supplementary notes are required –
- (i) [Code 1101] – The reason should be stated for any difference in the unearned premiums brought forward and the corresponding amount carried forward from the previous year – see paragraph 6 of Schedule 1. (i.e. if CAP 11.16.1 + CAP 11.16.2 does not equal CAP 11.19.2 in the previous return or CAP 11.16.3 + CAP 11.16.4 does not equal CAP 11.19.4 in the previous return).
 - (ii) [Code 1102] – The basis upon which the provision for unearned premiums is calculated and the reason for adopting that basis should be stated – paragraph 17 of Schedule 2. The Commissioner expects the reason stated to include an explanation of any change in the basis from previous years.
 - (iii) [Code 1103] – The supplementary note referred to in paragraph 107 above.

CAP 12 – Analysis of claims, expenses and technical provisions – accident year accounting

Completion of the Form

110. CAP 12 should be prepared separately for each accounting class. No summary form is required. The form presents an analysis of claims, expenses and technical provisions for business accounted for on an accident year basis.
111. Claims provisions and claims paid are analysed in some detail between incidents which occurred in previous financial years and those which incurred in the current financial year. Business which is shown as reconciliation business on CAP 13 should also be split between "prior financial years" and "this financial year". Where such amounts are not material, it is acceptable to include them in their entirety under the "this financial year" heading.
112. Amounts included at lines 11 to 18 are to be shown undiscounted and related adjustments for discounting are to be shown at lines 31 to 39.
113. The values in column 4 are calculated as follows:
- for lines 11 to 18, values in column 2+3-1
 - for lines 21 to 29 and lines 41 and 42, values in column 1+2-3
 - for line 19, lines 31 to 39 and lines 51 and 52, values in columns 3-1.
114. Amounts shown at lines 11 to 13, lines 15 to 17 and lines 31 and 32 shall exclude amounts in respect of claims management costs.



115. The amounts included for the provision for unexpired risks (at line 19), for any accounting class, should be determined without taking into account any surplus expected to arise on the unexpired risks falling within other accounting classes.
116. However, in determining the total provision for unexpired risks (which is disclosed in CAP 5 at line 13 and in CAP 4 at line 63), deficits and surpluses in different accounting classes may be offset (to the extent permitted by generally accepted accounting practice). Any surplus for an accounting class thus offset against deficits in other accounting classes, to the extent it relates to business accounted for on an accident year basis, should be shown as a negative provision at line 19 for that accounting class.
117. Lines 41 and 42 show the split of operating expenses between prior financial years and this financial year. Special care should be taken when completing column 1 – amount brought forward from previous financial years. The entry at column 1 for line 42 should equal the sum of the entries at column 3 in the previous years' return for lines 41 and 42. The entry at column 1 for line 41 should ordinarily be nil, i.e. it should be left blank. This is because the split at lines 41 and 42, column 4 is used (on CAP 10) to match expenses against earned premiums.

Supplementary Notes

118. Six supplementary notes are required –
- (i) [Code 1201] – If any amounts brought forward from previous years do not equal those carried forward in last year's return, the reason should be stated – paragraph 6 of Schedule 1.
 - (ii) [Code 1202] – The basis for determining the claims management costs payable and carried forward should be stated – paragraph 21(1) of Schedule 2. The "payable" part of the disclosure should include an explanation as to how overheads are allocated between "claims management expenses" and "net operating expenses". If claims outstanding are carried forward without a corresponding figure for claims management costs, the reason for this should be stated – paragraph 21(2) of Schedule 2. If the insurer has ceased to write a certain class of business, the basis for calculating any additional costs, or the reason for believing there should not be any, should be stated – paragraph 21(3) of Schedule 2.
 - (iii) [Code 1203] – Where investment income has been taken into account in determining the claims management costs carried forward, the insurer should state for each accounting class (i) the rates of interest used, and (ii) the average interval to the date at which the carried forward costs are expected to be expended – paragraph 21(4) of Schedule 2.
 - (iv) [Code 1204] – The basis for determining acquisition expenses (other than commission) payable and carried forward should be stated – paragraph 22 of Schedule 2. The "payable" part of the disclosure should include an explanation as to how overheads are allocated between "other acquisition expenses" and the other components of "net operating expenses" especially "administrative expenses". The "carried forward" part of the disclosure should include an explanation of how the appropriate proportion of acquisition expenses (other than commission) to match the unearned premium carried forward was determined.
 - (v) [Code 1205] – Where the provision for unexpired risks has been determined after taking investment income into account, an insurer

should state for each accounting class (i) the provision before taking investment income into account, (ii) the rates of interest used, and (iii) the average interval to the date at which claims are expected to be settled in cash – see paragraph 19 of Schedule 2. This note should be present even if, as a result of taking investment income into account, the provision for unexpired risks is Nil.

- (vi) [Code 1206] – If the amounts to be recovered from reinsurers are not expected to be recovered for more than 12 months after the settlement of the gross claims, there should be stated for that accounting class (i) the amount of such recoveries, and (ii) the accounting treatment which has been adopted in respect of discounting such recoveries – paragraph 27 of Schedule 2.

CAP 13 – Analysis of net claims and premiums – accident year accounting

Completion of the Form

119. CAP 13 should be prepared separately for each accounting class. No summary form is required. The form presents an analysis, by accident year, of the run-off of net claims and premiums. It consists of 3 parts.
- the last 3 accident years (lines 11 to 13);
 - the prior accident years (line 21); and
 - the reconciliation business (line 22).
120. All figures are to be shown net of the reinsurers' share. The accident years shown at lines 11 to 13 shall correspond to this financial year and the two previous financial years respectively.
121. Columns 1 to 6 are to be shown before deduction for discounting. All amounts shown shall exclude claims management costs.
122. CAP 13.29.2 + CAP 13.29.3 = CAP 12.13.3 + CAP 12.17.3.
 CAP 13.29.4 + CAP 13.29.5 = CAP 12.13.1
 CAP 13.29.7 = CAP 12.31.3 – CAP 12.32.3
 CAP 13.29.1 = CAP 12.13.2 + CAP 12.17.2
123. The amount of earned premiums shown at column 8 for each accident year should be updated each financial year to take account of overestimates or underestimates of premium for that accident year.
124. Reconciliation business is mainly any business which was reported as reconciliation business under the 1996 Regulations.
125. Special rules apply to the reversion of the premium amounts in column 8. All amounts denominated in a foreign currency (US dollars, Canadian dollars and any other currency the insurer wishes to treat as a major currency) should be reconverted into sterling using the exchange rate ruling at the end of the current financial year. Amounts denominated in a non-major currency need not be reconverted. Where a premium amount is not reconverted, it should be reported at the exchange rate which ruled at the end of the financial year in which it first arose.

Supplementary Notes

126. Two supplementary notes are required –

- (i) [Code 1301] – If any of the brought forward amounts differ from the corresponding carried forward amounts in the previous return, the reason should be stated – paragraph 6 of Schedule 1.
- (ii) [Code 1302] – If during the financial year, business is transferred (under Schedule 10 of the Ordinance or under equivalent legislation of an EEA State) to the insurer, certain specified details of that business must be stated – paragraph 16 of Schedule 2.

CAP 14 – Analysis of premiums, claims and expenses – underwriting year accounting

Completion of the Form

- 127. CAP 14 is only relevant for business accounted for on an underwriting year basis and should be prepared separately for each accounting class. The form reconciles the technical provisions brought forward to that carried forward, with premiums, claims, expenses and profits/losses as the reconciling items.
- 128. The column headings (between columns “29-29” and “99-99”) should be completed respectively from right to left with the dates of the end of this financial year and each of the two preceding financial years.
- 129. For accounting classes 1 to 8 and 10, amounts in respect of underwriting years ended before 31 December 1995 shall be included in the prior years column.
- 130. The amounts shown at lines 11 to 49 shall be the amounts payable or receivable during this financial year. Amounts shown at lines 21 to 29 shall exclude claims management costs.
- 131. In lines 11 and 12, premium amounts have to be shown gross of commission. Net operating expenses (lines 41 to 49) should not include the increase or decrease in deferred acquisition costs (“DAC”). Instead, the DAC brought forward and carried forward should be included respectively at lines 51/52 and 53/54 (DAC is part of the fund – see line 24 on CAP 15).
- 132. For an open underwriting year, line 54 (“Technical provisions – carried forward – adjustment for discounting”) should show the extent to which future investment return has been taken into account in deciding whether and, if so, by how much to increase the “fund” (i.e. premiums written less claims and expenses) to make it sufficient to meet all present and future obligations attributable to the underwriting year, (i.e. the amount shown at line 53 (“Technical provisions – carried forward – undiscounted”) should be the “fund” augmented by the full amount needed to make it sufficient to meet all such obligations without taking future investment return into account).
- 133. The amount shown at line 54 for an open year should be included as one of the component items included in the balance shown at line 20 on CAP 15, even if that results in a negative amount at that line (lines 16 to 18 on CAP 15 should not include amounts for open underwriting years).

Supplementary Notes

- 134. Six supplementary notes are required -
 - (i) [Code 1401] – If any of the brought forward amounts differ from the corresponding carried forward amounts in the previous return, the reason should be stated – paragraph 6 of Schedule 1.
 - (ii) [Code 1402] – Certain specified details of the reporting basis and the basis of profit recognition should be stated – paragraph 23 of Schedule 2.



- (iii) [Code 1403] – If, during the financial year, business is transferred (under Schedule 10 of the Ordinance or under equivalent legislation of an EEA State) to the insurer, certain specified details of that business must be stated – paragraph 16 of Schedule 2.
- (iv) [Code 1404] – The basis for determining the claims management costs payable and carried forward should be stated – paragraph 21 of Schedule 2. The “payable” part of the disclosure should include an explanation as to how overheads are allocated between “claims management costs” and “net operating expenses”. If claims outstanding are carried forward without a corresponding figure for claims management costs, the reason for this should be stated. If the insurer has ceased to write a certain class of business, the basis of calculating any additional costs, or the reason for believing there should not be any, should be stated.
- (v) [Code 1405] – Where investment income has been taken into account in determining the claims management costs carried forward, the insurer should state for each accounting class (i) the rates of interest used, and (ii) the average interval to the date at which the carried forward costs are expected to be expended – see paragraph 21(4) of Schedule 2.
- (vi) [Code 1406] – The basis for determining acquisition expenses (other than commission) payable and carried forward should be stated – paragraph 22 of Schedule 2. The “payable” part of the disclosure should include an explanation as to how overheads are allocated between “other acquisition expenses” and the other components of “net operating expenses” especially “administrative expenses”. The “carried forward” part of the disclosure should include an explanation of how the appropriate proportion of acquisition expenses (other than commission) to match the unearned premium carried forward was determined.

CAP 15 – Analysis of technical provisions – underwriting year accounting

Completion of the Form

- 135. CAP 15 is relevant only for business accounted for on an underwriting year basis and should be prepared separately for each accounting class. The form analyses the technical provision carried forward and has been designed to deal with both open and closed underwriting years, and both annual and non-annual methods of accounting.
- 136. The guidance given for the completion of CAP 14 also applies for this form.
- 137. The extent to which the form is to be completed differs for “open” and “closed” years – lines 11 to 15, 19 to 21 and 29 shall be completed for open years and lines 11 to 18 and 21 to 29 for closed years. (For this purpose, business accounted for under the annual method should be regarded as “closed year” business). Claims outstanding and IBNR, plus claims management costs, should be shown for “open” and “closed” business.
- 138. Lines 11 to 15 are to be shown before adjustment for discounting. Lines 11 to 14, 16 and 17 shall exclude claims management costs.
- 139. For accounting classes 1 to 8 and 10, all amounts in respect of financial year ended before 31 December 1995 should be included in the prior underwriting years column.

140. The offset of surplus and deficits on open years for business managed together should be shown at line 19 with a surplus on the underwriting year, which is to be offset against deficits arising elsewhere, shown as a positive amount and a deficit, which is to be offset against surpluses arising elsewhere, shown as a negative amount. The balance of the fund should be shown at line 20. For open years, there will be no entries in lines 22 to 25. Line 21 should equal line 29, which should equal line 53 less line 54 on CAP 14. The balancing figure required to achieve this should be entered at line 20.
141. Further disclosure needs to be given in relation to closed years, in particular, the adjustment for discounting (lines 16 to 18) and lines 22 to 25. The amount included for the provision for unexpired risks (line 23), for any accounting class, should be determined without taking into account any surplus expected to arise on the unexpired risks falling within other accounting classes.
142. In determining the total provision for unexpired risks (which is disclosed in CAP 5 at line 13 and in CAP 4 at line 63), deficits and surpluses in different accounting classes may be offset (to the extent permitted by generally accepted accounting practice). Any surplus for an accounting class thus offset against deficits in other accounting classes, to the extent it relates to business accounted for on an underwriting year basis, should be shown as a negative provision at line 23 on CAP 15 for that accounting class.
143. Lines 13 and 14 refers to both open and closed years to "claims incurred but not reported". For closed years, this does not include provisions for claims not incurred, i.e. claims expected to be incurred after the end of the financial year. For closed years, such yet-to-be incurred expected claims are provided against by the provision for unearned premiums and unexpired risks (lines 22 and 23). For open years, such yet-to-be incurred expected claims may either be included at lines 13 and 14 or included as one of the elements represented by the balance of the fund (line 20). For both open and closed years, lines 13 and 14 require the analysis of "claims incurred but not reported" between the "gross amount" and "reinsurers' share".
144. A summary of the lines which require completion in respect of open and closed years is as follows:-

| <u>Lines</u> | <u>Open</u> | <u>Closed or annual basis</u> |
|--------------|-------------|-------------------------------|
| 11 to 14 | ✓ | ✓ |
| 15 | | ✓ |
| 16 to 18 | | ✓ |
| 19 to 20 | ✓ | |
| 21 | ✓ | ✓ |
| 22 to 25 | | ✓ |
| 26 | ✓ | ✓ |

Supplementary Notes

145. Five supplementary notes are required –
- (i) [Code 1501] – The basis upon which the provision for unearned premiums is calculated and the reason for adopting that basis should be stated – see paragraph 17 of Schedule 2. The "reason" stated must include an explanation of any change in the basis from previous financial years.



- (ii) [Code 1502] – Where investment income has been taken into account in determining the provision for unexpired risks, the insurer must state for each class of business (i) the provision before taking investment income into account, (ii) the rates of interest used, and (iii) the average interval to the date at which claims are expected to be settled in cash. The note should be present even if, as a result of taking investment income into account, the provision for unexpired risks is nil – paragraph 19 of Schedule 2.
- (iii) [Code 1503] – If the amounts to be recovered from reinsurers are not expected to be recovered for more than 12 months after the settlement of the gross claim, the note should state for each accounting class (i) the amount of such recoveries, and (ii) the accounting treatment adopted in respect of discounting such recoveries – paragraph 27 of Schedule 2.
- (iv) [Code 1504] – Where a surplus for offset is shown at line 19, the following should be stated –
- a description of the business in respect of which the anticipated surplus, and of the business in question in respect of which the anticipated deficit to be offset, arise; and
 - the reason for treating the business as managed together
- Paragraph 24(2) of Schedule 2.
- (v) [Code 1505] – Particulars of any amounts included at lines 25 on CAP 15 should be stated.

Regulation 19, 20 And 21 Statements: Major Treaty Reinsurers, Major Facultative Reinsurers And Major Cedants

General

146. Regulations 19, 20 and 21 require the submission of additional information with regards to major treaty reinsurers, major facultative reinsurers and major reinsurance cedants, respectively. These statements are intended to give information on the insurer's exposure to particular treaty and facultative reinsurers where they are material, and also on the major sources of the insurer's inward treaty reinsurance business. All of the statements are subject to audit.
147. All three statements require the following information:
- full name and address of reinsurer/cedant;
 - whether (and, if so, how) the reinsurer/cedant was connected with the insurer during the year;
 - reinsurance premiums payable/gross premiums receivable from the reinsurer/cedant during the year; and
 - the amounts of any debts/deposits received, and recoveries anticipated, which are included in the return as follows.
 - (i) Regulation 19/20
 - Debts due: CAP 4 line 74.
 - Deposit received: CAP 5 line 31.



Recoveries included in reinsurers' share of technical provision:
CAP 4 line 62.

(ii) Regulation 21

Deposit made: CAP 4 line 51.

Debt due: CAP 4 line 73.

148. If the insurer has no disclosable major treaty reinsurers, major facultative reinsurers or major cedants, the Regulation 19, 20 or 21 statement should state that this is the case.

Major treaty reinsurers

149. Regulation 19 requires every insurer which carries on general business to prepare a statement of its major treaty reinsurers. The items to be included in that statement are listed in regulation 19(1).

150. Regulation 19(2) lays down two tests for identifying major treaty reinsurers –

- a premium ceded limit; and
- a debt plus anticipated recoveries limit.

151. A major treaty reinsurer is any reinsurer which either exceeds the "premium ceded" limit in the current or any of the five immediately preceding financial years or exceeds the "debt plus anticipated recoveries" limit at the current year end. The limits are applied in aggregate, (i.e. to the sum of all amounts from all treaties ceded to that reinsurer), except that the premium ceded limit is applied separately for, and differs in respect of, proportional and non-proportional treaty aggregates.

152. The "premium ceded" limits are –

- for proportional treaty reinsurance, 2% of the total gross premium written of the insurer;
- for non-proportional treaty reinsurance, 5% of the total premium payable in respect of all non-proportional reinsurance.

153. The "debt plus anticipated recoveries" limit is 5% of the insurer's GBA. (See Guidance Note No. 4 on the Valuation of Assets which explains how the GBA is calculated). The "debt plus anticipated recoveries" which are compared with this limit should include the amount of any debt due or reinsurance recovery anticipated from the reinsurance in respect of treaty reinsurance ceded, but only to the extent that they are taken into account in CAP 4 (lines 62 and 74), i.e. net of any specific bad or doubtful debt provision. Further, the anticipated recoveries need only be included to the extent they arise from the reinsurer's share of the gross provision for notified outstanding claims, and IBNR claims arising from specific occurrences (e.g. hurricane, earthquake) to which provisions have been allocated.

154. If two or more reinsurers are connected to each other, the "premium ceded" and "debt plus anticipated recoveries" limits should be compared to their total business. If either limit is exceeded, all the connected reinsurers should be considered major treaty reinsurers and the items referred to in regulation 19(1) listed separately for each.

Major facultative reinsurers

155. Regulation 20 requires every insurer which carries on general business to prepare a statement of its major facultative reinsurers. The items to be included in that statement are listed in regulation 20(1).

156. The definition of major facultative reinsurer and the items to be included in the statement are similar to that for the major treaty reinsurers. The differences are explained below.
157. The “premium ceded” and “debt plus anticipated recoveries” limits are applied separately for each facultative reinsurance contract. The items to be stated for the major facultative reinsurer need only to be in respect of the major facultative reinsurance contract (and, if there is more than one major facultative reinsurance contract for that reinsurer, should be stated separately for each). Other (smaller) facultative reinsurances of the same reinsurer may be ignored.
158. The “premium ceded” limit is ½% of total gross premiums written. The “debt plus anticipated recoveries” limit is 1% of the GBA. A major facultative reinsurance is a facultative reinsurance which exceeds either limit in the current financial year. [Note - unlike for treaty reinsurance, there is no reference back to the five preceding financial years in applying the “premium ceded” limit. Nor are connected reinsurers aggregated in applying either limit.]

Major cedants

159. Regulation 21 requires every insurer which carries on general business to prepare a statement of its major cedants. The items to be included in that statement are listed in regulation 21(1).
160. A major cedant is any insurer from which the gross premiums written in respect of the total business accepted under treaty reinsurances exceeds the greater of –
- 5% of total gross premiums written under all treaty reinsurances accepted; or
 - 2% of gross premium written from all sources, for the current or any of the three immediately preceding financial years.
161. If two or more cedants are connected, the above limits should be compared to their total business. If either limit is exceeded, all the connected cedants should be considered major cedants and the items referred to in paragraph 159 above separately listed for each.

Connected companies

162. Regulation 22 defines when companies should be regarded as connected for the purposes of regulations 19 to 21. The need to define “connected” arises in two contexts
- firstly, as explained above in identifying major treaty reinsurers and major cedants, reinsurers connected to each other and cedants connected to each other are respectively grouped.
 - secondly, one of the items to be disclosed in respect of each major treaty reinsurer, major facultative reinsurer and major cedant is whether (and, if so, how) it is connected to the insurer.
163. The test of connectedness differs somewhat for these two uses. In both uses, a person (i.e. individual or body corporate) and a body corporate are considered connected if the person is –
- a subsidiary undertaking of the body corporate;
 - a parent undertaking of the body corporate; or

- a subsidiary undertaking of a parent undertaking of the body corporate.
164. In the second use, a person and body corporate would also be considered connected if one of them is controlled by the other; or they are both controlled by the same person. For these purposes, a special definition of control applies – see regulation 22(2) and (3) which define control for these purposes.
165. Both the above definitions of “connected” are subject to the exception that a person and body corporate are not be considered connected if the reporting insurer –
- does not know, and
 - could not upon reasonable enquiry be expected to find out, that the connection exists.
166. Other than in exceptional circumstances, the reporting insurer should know of any connections between its reinsurers (or cedants) and itself or companies with which it is connected. However, the insurer making the return may not be aware in all cases of connections between its reinsurers (or cedants) where they are not, in turn, connected to the insurer. In order to comply with the requirement to make “reasonable enquiry”, it will suffice for the insurer making the return to refer to the latest available published accounts etc. (provided that, in all cases, the source to which reference is made has been published within twelve months of the end of the financial year to which the return relates). Alternatively, the insurer may request any or all of its reinsurers (or cedants) to provide details of their connected companies. If no information is available from acceptable published material, or obtained in response to a specific approach to a reinsurer (or cedant), the Commissioner takes the view that, in the usual case, the obligation to make a “reasonable enquiry” will have been satisfied, and, should the information be found to be inaccurate or incomplete, no offence will have been committed under the Ordinance by the insurer making the return. (However, possible breaches of the Regulations will need to be considered case by case. The foregoing is, therefore, only a general guide to the Commissioner’s likely attitude).
167. The above rules do not apply in respect of reinsurers who are members of Lloyd’s. For the purposes of preparing the Regulation 19, 20 and 21 statements, all members of Lloyd’s are taken as a whole.

Nil returns

- 167A. Where there are no disclosable major treaty reinsurers, major facultative reinsurers or major cedants, the statements should state that this is the case.

The Regulation 26 / Schedule 5 Statement: Business Ceded

Overview

168. The Schedule 5 statement which must be prepared is not subject to audit. It is intended to give an overview of the insurer’s outward non-facultative reinsurance protections. Its minimum contents are prescribed in paragraphs 1 to 5 of Schedule 5 which provide as follows.

Paragraphs 1 and 2

169. Paragraph 1 requires a description to be given for each outward non-facultative reinsurance contract entered into, or modified, during the financial year. The description includes –
- type of business covered by reference to risk groups or business categories;
 - type of cover;
 - policy limits, including number of reinstatements and aggregate limits; and
 - period of cover.

You should refer to the text of paragraph 1 for a fuller description of the disclosure required.

170. A contract is “modified” when the terms of the original contract are altered by mutual agreement of the parties. If one party exercises an option (e.g. to extend cover) which is contained in the original policy, this does not constitute a “modification”. The existence of the option should be disclosed in the “type of cover” description given at the time when the policy was originally disclosed.
171. Information on contracts modified during the financial year need only be given if the modification renders the information originally disclosed either inaccurate or materially incomplete. Modifications of contracts originally entered into prior to the first financial year covered by these returns need not be reported.
172. The lay-out and presentation of the information required by this paragraph is at the discretion of the insurer provided that it is “fairly presented” (see regulation 5), legible and complete. In particular, the information may be presented, wholly or in part, in the form of a table or chart. However, information on reinsurances which cover the same type of business for similar periods of cover is laid out together.

Paragraph 3(a)

173. This sub-paragraph requires extra disclosure for outward reinsurance contracts which are subject to no, or a finite number of, reinstatements. Where it is anticipated that claims arising from incidents which occurred during or prior to the financial year will fully exhaust the reinsurance (including all reinstatements) this should be disclosed.
174. The disclosure is required for any reinsurance reported under paragraph 6 whether in the present or previous returns, but not reinsurances only reported on Form INS 30 of the 1996 Regulations. The disclosure need only be given once, i.e. if a particular reinsurance is reported under paragraph 3(a), it need not be so reported under the paragraph in subsequent returns.

Paragraph 3(b) and (c)

175. These sub-paragraphs require extra disclosure where reinsurers representing a 10% or more participation in any reinsurance have “ceased to pay claims to their reinsureds in full”. This refers to where a reinsurer ceases to pay claims in full, as they fall due, to all or substantially all of its reinsureds. It does not require that the reinsurer should have actually refused to pay (in full) the particular insurer preparing the return. Nor does it include situations where the reinsurer is refusing to pay that particular insurer (e.g. due to a dispute) but is continuing to pay the general body of its reinsureds.



176. The cessation of claims payment in full referred to would typically arise where the reinsurer is in liquidation, provisional liquidation, or is paying less than 100% of claims under the provisions of a scheme of arrangement (or is subject to similar insolvency processes under the laws of other countries). However, it would also include situations where the reinsurer was operating a claims-moratorium outside the protection of a formal insolvency legal process.
177. The disclosure under these sub-paragraphs is required for any reinsurance reported under paragraph 8 above, whether in the present or previous returns, but not reinsurances only reported on Form INS 30 of the 1996 Regulations.
178. The disclosure should identify the reinsurance contract and state the participation in that reinsurance represented by reinsurers which have ceased to pay claims in full. [But it is not necessary to name those reinsurers.] Once this disclosure has been made for a particular reinsurance contract, it need not be repeated in subsequent returns unless, due to further reinsurers ceasing to pay claims in full, the percentage has increased by more than 10%.
179. The percentage to be disclosed is the full percentage participation for a reinsurer even if that reinsurer is still making partial payments on claims. For example, if ABC Reinsurance Co. has a 10% line on a reinsurance policy and ABC is now paying claims at 60 pence in the pound, the full 10% should be disclosed. The fact that 60 pence in the pound on that 10% participation, is still being paid may also be disclosed, but there is no requirement to do so.

Paragraph 4

180. This paragraph requires disclosure of the insurer's maximum probable loss (net of reinsurance) (MPL) from –
- any one contract; and
 - all contracts taken together.
181. The disclosure is required separately for each risk group or business category, or part thereof, in respect of which separate non-facultative reinsurance cover has been obtained. The disclosure is required for a risk group or business category even if no reinsurance has been obtained for that risk group or business category.
182. A separate MPL for every non-facultative reinsurance policy is not required. Only one MPL, on each of the bases "any one contract effected by the insurer" and "all contracts taken together", should be disclosed for each group, business category or part thereof as described in the above paragraph. The MPL should be net of all reinsurance protecting the risk group, business category or part thereof.
183. The MPL should not be confused with the deductible or retention on the insurer's lowest level of reinsurance protection. It may only equal that amount where (i) the maximum probable gross loss is not expected to exceed the reinsurance protection; (ii) the reinsurance protection is fully placed, i.e. no co-reinsurance; and (iii) recovery from the reinsurance protection does not result in liability for additional premiums.
184. Sub-paragraph (2) defines maximum probable net loss. It, amongst other things, refers to "any one incident or series of incidents arising from the same originating cause". This wording is intended to require the aggregation of losses from a single incident, or series of incidents, where the MPL's would have to be aggregated for the purpose of making recoveries on the insurer's (higher layers) reinsurance. It is self-evident that this "all contracts taken together" MPL cannot be less than the "any one contract" MPL.

Paragraph 5

185. This paragraph requires that the split of reinsurance premiums (as shown on CAP 11 and CAP 14) for each accounting class between facultative and non-facultative reinsurance be disclosed.

The Regulation 24 Statement: Shareholder Controllers

186. The Regulation 24 statement is only required for an insurer which falls within the definition of section 2(2) of the Ordinance of "Gibraltar insurer" which is an insurance company –
- which is incorporated in, has its head office in, and is licensed in Gibraltar; and
 - whose business is not restricted to reinsurance.
187. Regulation 24 requires a list of all persons who, to the insurer's knowledge, were at any time during the financial year shareholder controllers of the insurer together with their percentage shareholding and voting power at the end of the financial year in the insurer (or in another company of which the insurer is a subsidiary undertaking).
188. The duty to list shareholder controllers under Regulation 24 is separate and distinct from the requirement to notify those persons under sections 41 to 44 to the Ordinance. Including such a person in the Regulation 24 list does not relieve him/her of the duty to make notifications under those sections or vice versa.
189. A shareholder controller is defined by section 2(16) of the Ordinance as any person who either alone or with any associate or associates –
- holds 10 per cent or more of the shares in the insurer, or another company of which it is a subsidiary undertaking;
 - is entitled to exercise, or control the exercise of, 10 per cent or more of the voting power at any general meeting of the insurer or another company of which it is a subsidiary undertaking; or
 - is able to exercise a significant influence over the management of the insurer or of another company of which it is such a subsidiary undertaking by virtue of –
 - (i) a holding of shares in; or
 - (ii) an entitlement to exercise, or to control the exercise of, the voting power at any general meeting of,
 the insurer or, as the case may be, that other company.
- In the statement for an insurer that is part of a group with more than one intermediate holding company, there may be several levels of shareholder controllers to list since each intermediate holding company has to be reported.
190. For the above, an "associate" of a person is –
- the wife or husband or minor son or daughter of that person;
 - the trustees of any settlement under which that person has a life interest in possession;
 - any company of which that person is a director;
 - any person who is an employee or partner of that person;
 - if that person is a company –

- (i) any director of that company;
 - (ii) any subsidiary undertaking of that company;
 - (iii) any director or employee of any such subsidiary undertaking; and
- any other person with whom that person has made an agreement or arrangement –
 - (i) with respect to the acquisition, holding or disposal of shares or other interests in the company concerned or another company of which it is a subsidiary undertaking; or
 - (ii) under which they undertake to act together in exercising their voting power in relation to the company concerned or another company of which it is such an undertaking.
191. Further guidance on the definition of shareholder controller is given in Insurance Guidance Note No. 3.
192. The percentage shareholder and voting rights to be disclosed in the Regulation 24 statement should include the holding/rights of associates.
193. Where there are no shareholder controllers to report, the Regulation 24 statement should state this.
194. A suggested proforma is at Annex 1, but it is not necessary to use it.

Certificates By Directors And Reports Of Auditors

Certificate by the directors etc.

195. Part I of Schedule 6 to the Regulations specifies the statements to be included in the directors' certificate.
196. Where, in the opinion of those signing the certificate, the circumstances are such that any of the statements required by paragraphs 1 to 6 of the Schedule cannot truthfully be made, the relevant statements shall be omitted, (see paragraph 7(1) of the Schedule). Where any statements have been omitted, this fact shall be stated in a note, (see paragraph 7(2) of the Schedule) and reasons given.
197. Paragraph 5 of Part I of Schedule 6 covers directors' certificates in respect of two types of published guidance – "systems of control" and "preparation of returns" guidance. The Commissioner will circulate from time to time a list of the published guidance which he considers relevant for this purpose.
198. In order to certify compliance with "systems of control" guidance, it is necessary for the directors to be satisfied that the control system was in place at the end of the financial year in question, and that it was reasonable to believe that the systems continued to be in place after that date, and will continue to be in place for the foreseeable future. In this instance, the beliefs which the directors hold at the time of signature of the returns are the relevant ones. For example, if the system was believed to be in place at the end of the financial year in question, had clearly – but unexpectedly – failed shortly afterwards and was once again believed to be in place at the time of signature of the returns, the certificate could not properly be given.
199. As to the standard of compliance required, the Commissioner recognises that absolute assurance is most unlikely to be achieved. By way of illustration, an isolated human error would not of itself be considered a failure of the system provided that the system is capable of recognising and rectifying the error

swiftly. Frequent or repeated errors would, however, cast doubt on the integrity of the system.

200. A list of the guidance complied with is sufficient. Where only part of a published guidance note is complied with, it is acceptable to claim compliance with that part. Where directors do not know or cannot satisfy themselves, whether guidance has been complied with, such guidance should be omitted from the list. It is not necessary to state which guidance has not been complied with, except in rare cases when no published guidance has been complied with (in which case the negative disclosure referred to in paragraph 196 above comes into play).
201. An example certificate is attached as Annex 2.

The auditors' report

202. Regulation 29 specifies the scope of the audit. The contents of the auditors' report are set out in Part III of Schedule 6. Section 47 of the Ordinance specifies the qualifications of an auditor.
203. The Auditing Practice Board in the UK issues separate guidance notes specifically for auditors of insurance companies and it is recommended that auditors should refer to these.
204. The parts of the abbreviated return which are subject to audit are –
- CAP 1 to CAP 6 and CAP 10 to CAP 15; and
 - the statements furnished under regulations 19, 20 and 21.
205. The unaudited parts of the return are the statements furnished under regulations 24 and 26.
206. The auditors report must state whether the Director's certificate (except to the extent it refers to the unaudited parts of the returns) has been properly prepared in accordance with the Regulations, and whether or not it was unreasonable for the persons giving that certificate to have made the statements contained in it. Paragraph 11 provides that, to the extent that the information and explanations the auditors have received do not allow them to express this opinion, they should add to their report "such qualification, amplification or explanation as may be appropriate".
207. The Commissioner considers that it is appropriate for compliance with most, but not necessarily all, relevant published guidance to be subject to the audit opinion described above. When, periodically, a list of relevant published guidance is circulated, the Commissioner will make clear whether or not he would normally expect an audit opinion in respect of compliance with that guidance. Where audit of compliance with a guidance note is inappropriate (or has not been carried out for some reason), the auditor would be expected to invoke paragraph 11 of Schedule 6 to record the fact.
208. Paragraph 12 of Schedule 6 provides that, where the auditors refer in their report, or in any note attached thereto, to any uncertainty, the report shall also state whether, in the auditor's opinion, that uncertainty is material to determining whether the insurer has available assets over the appropriate solvency margin. This paragraph should not be read as requiring the auditors to refer to an uncertainty. It merely provides that, if they do so, an additional opinion is required. The Commissioner expects an uncertainty to be treated as material for these purposes if, upon the crystallisation of so much of the uncertainty as is not remote, the required level of available assets would not be met.



209. An example report is attached as Annex 3. It is also recommended that auditors should become familiar with APB Bulletin 1998/3 on "Auditors' Reports on Regulatory Returns made under the Insurance Companies Act 1982."



Annex 1: Statement of Shareholder Controllers

Returns for the year ended (Date)

Statement in accordance with regulation 24 of the Insurance Companies (Accounts and Statements) Regulations 1998

Additional information on shareholder controllers

We confirm the following is a list of:

- (a) Persons who, to the knowledge of the company, have been, at any time during the year ended (Date), a shareholder controller of the company; and
- (b) In the case of each person who was a shareholder controller of the company at (Date):
 - (i) the percentage of shares he held at that time in the company, or in another company of which the company was a subsidiary undertaking; and
 - (ii) the percentage of the voting power which he was entitled at that time to exercise, or control the exercise of, at any general meeting of the company, or another company of which it was a subsidiary undertaking;

in each case, either alone or with any associate or associates.

| Persons who, to the knowledge of the company, have been, at any time during the year ended (Date), a shareholder controller of the company. (Please show date ceased to be a shareholder controller, if applicable). | In the case of each person who was a shareholder controller of the company at (Date): | |
|---|---|---|
| | The percentage of shares he held at that time in the company, or in another company of which the company was a subsidiary undertaking, either alone or (shown separately) with any associate or associates. | The percentage of the voting power which he was entitled at that time to exercise, or control the exercise of, at any general meeting of the company, or another company of which it was a subsidiary undertaking, either alone or (shown separately) with any associate or associates. |
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Annex 2: Example Certificate By Directors

We certify:

1. (a) that in relation to the part of the return comprising forms CAP 1 to CAP 6, CAP 10 to CAP 15 (including the supplementary notes thereto) and the statements required by regulations 19 to 21, 24 and 26 of the Insurance Companies (Accounts and Statements) Regulations 1998 (“the Regulations”):-
 - (i) the return has been prepared in accordance with the Regulations;
 - (ii) proper accounting records have been maintained and adequate information has been obtained by the insurer; and
 - (iii) an appropriate system of control has been established and maintained by the insurer over its transactions and records;
- (b) that reasonable enquiries have been made by the insurer for the purpose of determining whether any person and any body corporate are connected for the purposes of regulations 19, 20 and 21 of the Regulations; and
- (c) in respect of the company’s business which is not excluded by regulation 38 of the Insurance Companies (Valuation of Assets and Liabilities) Regulations 1996, the assets held throughout the financial year enabled the company to comply with regulations 33 to 37 (matching and localisation) of those Regulations.
2. that the margin of solvency required by section 59 of the Insurance Companies Ordinance 1987 has been maintained throughout the financial year.
3. (a) that the systems of control established and maintained by the insurer in respect of its business complied at the end of the financial year with the following published guidance:
 - (i) Insurance Guidance Note No. 5 – Systems of control over investments (and counterparty exposure) including the use of derivatives; and
 - (ii) Insurance Guidance Note No. 6 – Systems of control over general business claims provisions;and it is reasonable to believe that systems continued to so comply subsequently and will continue to do so in future.
- (b) that the return has been prepared in accordance with the following published guidance:
 - (i) Insurance Guidance Note No. 2A – The preparation of Annual Returns for general business insurers and reinsurers;
 - (ii) Insurance Guidance Note No. 2C – The use and preparation of abbreviated Annual Returns for captive insurers; and
 - (iii) Insurance Guidance Note No. 4 – Valuation of Assets.

Address and date

Signatures



Annex 3: Example Report Of The Auditors

Report of the Auditors to the Directors pursuant to regulation 29 of the Insurance Companies (Accounts and Statements) Regulations 1998.

XYZ Insurance Company Limited

Financial year ended

We have examined the following documents prepared by the company pursuant to section 50 of the Insurance Companies Ordinance 1987 ("the Ordinance") and the Insurance Companies (Accounts and Statements) Regulations 1998 ("the Regulations"):

- Forms CAP 1 to CAP 6 and CAP 10 to CAP 15 (including the supplementary notes thereto) ("the Forms");
- the statements required by regulations 19, 20 and 21 on pages [] to [] ("the statements"); and
- the certificate signed in accordance with regulation 28(a) on pages [] and [] ("the certificate").

In the case of the certificate, our examination did not extend to paragraph [] in relation to the statements required by regulations 24 and 26, concerning shareholder controllers and general business ceded.

Respective responsibilities of the company and its auditors.

The company is responsible for the preparation of an annual return (including the Forms, statements and certificate) under the provisions of the Ordinance and the Regulations. [The requirements of the Regulations have been modified by [an] Order[s] issued under section 113 of the Ordinance by the Commissioner of Insurance on [and.....]]. Under regulation 5, the Forms and statements are required to be prepared in the manner specified by the Regulations and to state fairly the information provided on the basis required by the Regulations. It is our responsibility to form an independent opinion as to whether the Forms and statements meet these requirements and, in the case of the certificate, whether it was or was not unreasonable for the persons giving the certificate to have made the statements therein, and to report our opinion to you.

Basis of opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board in the United Kingdom, as adopted by the Gibraltar Society of Chartered and Certified Accountancy Bodies. Our work includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Forms and statements. The evidence includes that previously obtained by us relating to the audit of the financial statements of the company for the financial year on which we reported on []. It also includes an assessment of the significant estimates and judgements made by the company in the preparation of the Forms and statements.

We planned and performed our work so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Forms and statements are free from material misstatement, whether caused by fraud or other irregularity or error, and comply with regulation 5.

In the case of the certificate, the work performed involved a review of the procedures undertaken by the signatories to enable them to make the statements therein, and does not extend to an evaluation of the effectiveness the company's internal control systems.



Opinions

In our opinion:-

- (a) the Forms and statements fairly state the information provided on the basis required by the Regulations [as modified] and have been properly prepared in accordance with the provisions of those Regulations; and
- (b) according to the information and explanations received by us:
 - (i) the certificate has been properly prepared in accordance with the provisions of the Regulations; and
 - (ii) it was not unreasonable for the persons giving the certificate to have made the statements therein.

Auditors
Date
Address

Annex 4: Intra-Group Transactions

Supplementary note to CAP 10

1. Regulation 18A requires an insurer that has agreed to, or carried out, a material connected-part transaction to provide a supplementary note describing it to CAP 10 (for a transaction relating to general insurance business). The reference code should be 1006.
2. The Commissioner expects insurers to inform him about transactions with other group members who are significant for regulatory purposes even if they do not strictly fall within the reporting requirement under regulation 18A.

Connected-party transactions

3. The scope of the phrase “connected-party” is wider than that of the insurance group to which the parent undertaking solvency calculation applies. A connected party includes:
 - the related undertakings of the insurer;
 - the immediate, intermediate and ultimate parent and participating undertakings of or in the insurer; and
 - the related undertaking of participating undertakings in the insurer.A connected party may also be a natural person who holds a participation in any of the undertakings noted above.
4. A connected-party transaction is defined as “the transfer of assets or liabilities or the performance of services by or to a connected person irrespective of whether or not a price is charged”. As such it includes (but is not limited to):
 - loans and similar advances to or from a connected person, including inter-company balances and other such operating arrangements,
 - investments in the securities or shares of the connected person purchased by the insurer,
 - investments in the securities or shares of the insurer purchased by the connected person,
 - guarantees issued to the connected person by the insurer (and other similar off-balance sheet transactions), or vice versa,
 - reinsurance cessions to and acceptances from the connected person,
 - agreements to share of costs of the connected person, or to share the costs of the connected person with a third party,
 - payment of commission (including profit-commission and commission on reinsurance premiums) and other acquisition costs to the connected person,
 - transfer of property to or from the connected person, including investments, land, equipment and debts, and
 - transfer of liabilities to or from the connected person, including transfers of business under Part IX of the Ordinance.
5. Dividends payable are not intended to be covered by the disclosure requirement unless they are part of a wider transaction (because they are already disclosed in the returns).

6. A series of transactions that may include intermediate stages with third parties, but are in substance a transaction involving a connected-party transaction, are likely to be a connected-party transaction.

Materiality

7. The materiality of transactions is determined by reference to the general business amount (GBA) for transactions relating to general insurance business. The price or consideration paid or received is not necessarily determinative of value for the purposes of assessing whether the transaction is a material connected-party transaction, since the real value of an inter-group transaction may be greater (see definition of material connected-party transaction).
8. Similar transactions, taken together, are material (for the purposes of regulation 18A if when combined they exceed 5% (in terms of price or value) of the GBA. For this purpose the measurement should be done at the time or times the transactions take place. Rather than make a precise measurement, an estimate may be used that is likely to be an underestimate of the business amount to avoid the risk of not reporting transactions that should be reported. In general similar transactions will include those of the same type with the same or another connected party. Transactions would normally be considered to be of the same type if they were combined in the same heading in the profit and loss account, balance sheet or note to the financial statements of the insurer, or from part of a connected series of transactions. However, other groups of transactions may be considered as similar even if they do not meet the above criteria.

Aggregation of disclosure

9. Regulation 18A(3) allows (but does not require) transactions with the same connected person to be disclosed on an aggregated basis unless separate disclosure is needed for a proper understanding of the effects of the transactions upon the financial position or profitability of the insurer.
10. Similar transactions (as described in 8 above) with the same connected person may be aggregated, for instance all reinsurance premiums paid to a connected person may be aggregated. However, different types of transactions may not be appropriate for aggregation. For instance it would not in general be appropriate to aggregate loans to a connected person with equipment sold to that connected person.
11. Transactions with different connected persons of the same type should not be aggregated. For instance, commissions paid to two or more connected persons should not be aggregated, even if they need to be taken together to establish materiality, since separate disclosure will normally be necessary for a proper understanding (regulation 18A(3)).
12. Regulation 18A does not allow an exemption from disclosure similar to that offered under Financial Reporting Standard No 8 'Related Party Disclosures' where the results of the insurer and connected person are reported in consolidated financial statements. Insurance groups may have an order under section 113 of the Ordinance allowing preparation of a consolidated Form INS 20. Insurers will nevertheless still need to disclose material connected-party transactions separately for each insurer member of the group. As this is a requirement of Article 8 of the Insurance Groups Directive, it is unlikely that the Commissioner would be able to waive the requirement of individual disclosure.

Disclosure

13. The information to be disclosed is set out in regulation 18A(2). The disclosure should be adequate to allow the reader of the returns to understand the



nature of the relationship of the insurer with the connected person, and the nature of the transaction and its effect upon the financial position and the performance of the insurer.

14. Disclosure should include the transactions during the period and any amounts unpaid or outstanding in respect of those transactions at the end of the period.
15. Consistent descriptions of transactions should be used in subsequent returns.
16. The name of each connected person should be stated in full.
17. Where disclosures under this regulation would merely duplicate disclosures reported under other supplementary notes (e.g. large counterparty exposures) a cross-reference to the other supplementary notes should fulfil the requirement.



Annex 5: The CAP Forms

CAP 1 to CAP 15 are attached.