Notice No : MAS 125
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NOTICE ON INVESTMENTS OF INSURERS

Introduction

1. This Notice is issued pursuant to section 64(2) of the Insurance Act (Cap. 142) ("the Act").

2. This Notice shall be read in conjunction with the provisions of the Act and the Insurance (Valuation and Capital) Regulations 2004 (G.N. No. S 498/2004) ("the Regulations").

3. This Notice applies to any insurer registered to carry on insurance business. It sets out the basic principles that shall govern the oversight of investment activities of an insurer and the investments of its insurance funds, and in the case of an insurer that is incorporated or established in Singapore, the investments of both its insurance funds and its shareholders' funds.

4. Paragraphs 8 to 20 shall not apply to captive insurers and marine mutual insurers.

5. Paragraphs 21 to 28 shall not apply to an insurer in respect of the part of any insurance fund established and maintained for its investment-linked policies under section 17(1A)(a) of the Act relating to the unit reserves of the policies of the fund.

Interpretation

6. For the purpose of this Notice:

   (a) "appointed actuary" means a person appointed as an actuary of a direct insurer registered to carry on life business, to perform such duties as may be prescribed pursuant to section 31 of the Act;

   (b) "certifying actuary" means a person appointed as an actuary of a direct insurer registered to carry on general business, or of a reinsurer registered to carry on life or general business to perform such duties as may be prescribed pursuant to section 37 of the Act;

   (c) "economic capital" means the capital needed by an insurer to satisfy its risk tolerance and support its business plans and which is determined from an economic assessment of the insurer's risks, the relationship of these risks and the risk mitigation in place;

   (d) "efficient portfolio management", in relation to a derivative transaction, has the meaning ascribed in paragraph 26 below;

(e) "hedging" means the reduction of investment risk through engaging in a transaction for a derivative on an investment where there is a high degree of negative correlation between the changes in value of the derivative and changes in value of the hedged investment;

(f) "liquid assets" means assets which are readily converted into cash at a value close to its fair price under normal market conditions; and

(g) "marine mutual insurer" has the same meaning as in regulation 2 of the Insurance (General Provisions and Exemptions for Marine Mutual Insurers) Regulations 2007.

7. The expressions used in this Notice shall, except where expressly defined in this Notice or where the context otherwise requires, have the same respective meanings as in the Act.

Board of Directors and Senior Management Oversight

8. An insurer shall ensure that its investment policy is formulated, established and approved by the board of directors. The insurer shall also ensure that its board of directors, at all times, exercises added oversight to ensure that the interests and rights of policy owners are not compromised.

9. For the purpose of overseeing an insurer's investment activities, an insurer shall seek the approval from its board of directors to establish a committee (the "Investment Committee"). The Investment Committee shall comprise:

(a) the principal officer and chief investment officer (or an officer in a similar capacity responsible for the investment functions); and

(b) in the case of a direct life insurer, the persons referred to in sub-paragraph (a) and the appointed actuary.

10. In the case of an insurer whose principal officer is solely responsible for the insurer's investment functions and where the nature, scale and complexity of the risks and investments of the insurer permit, the insurer may allow that principal officer to perform the role and duties of the Investment Committee as set out in this Notice, provided that in the case of a direct life insurer, the Investment Committee shall comprise both the principal officer and the appointed actuary.

11. A direct general insurer and reinsurer should consult the certifying actuary on investment-related matters for which the certifying actuary's expertise and experience would be useful.

12. At least annually, an insurer shall ensure that its board of directors reviews the adequacy and relevance of its investment policy - in terms of overall risk tolerance, long-term risk-return requirements and solvency position - in the light of the insurer's activities and risk profile.

Reports to the Board of Directors

13. An insurer shall ensure that the Investment Committee reports regularly, but no less than once every quarter, to the board of directors and the insurer shall also ensure that the reports on investment activities are prepared in a timely manner. If the board of directors delegates authority to the Investment Committee to make investment decisions on its behalf, the insurer shall ensure that the Investment Committee reports to each meeting of the board of directors on any and all decisions of material consequence made since the last meeting of the board of directors, but such report of the Investment Committee shall be no later than three months of it making the decision of material consequence.

14. In addition to the above reports, the insurer shall ensure that the Investment Committee also prepares reports for the board of directors, as soon as (and in any case, no later than 2 weeks after) any investment-related activity of material consequence arises, with details of the various issues and the impact on the funds and the insurer.

Duties of the Investment Committee

15. An insurer shall ensure that its investments are carried out in accordance with a investment policy of the insurer that has been approved by the board of directors, supervised or directed by the Investment Committee. The insurer shall ensure that its investment policy incorporates the main elements as set out in Appendix A. The duties delegated to the Investment Committee shall include, but not be limited to the following:

    (a) to review the investment policy of the insurer on a regular basis so that it remains appropriate, recognising among other things, changes in business in-force and the economic environment;
    (b) to ensure the investment policy is consistent with the asset-liability management strategies required to support new and existing products;
    (c) where the insurer establishes and maintains a participating fund, to ensure the investment policy of the participating fund, is consistent with the bonus and dividend policy of the insurer;
    (d) to ensure the risk management functions continue to be appropriate;
    (e) to review the adequacy of internal control systems to support investment activities; and
    (f) to ensure resources dedicated to the investment activities of the insurer are sufficient to implement and manage the approved investment policy and any other activities requested by the board of directors.

16. An insurer shall ensure that its Investment Committee is in a position to monitor the performance of those managers against its approved policies and procedures.

17. An insurer shall ensure that the Investment Committee implements and maintains adequate risk management systems and controls in respect of the investments of the insurer. These shall include, but not be limited to, ensuring that:

    (a) there is proper segregation of execution, monitoring and performance measurement functions;
    (b) the authority of persons entering into, performing or otherwise dealing in investments for and on behalf of the insurer, and limits of such authority, are clearly delineated;
    (c) there are proper performance monitoring procedures;
    (d) there are continuous risk monitoring procedures;
    (e) there is timely management reporting;
    (f) the investments of the insurer are handled by qualified and properly trained persons capable of assessing the nature, scale and complexity of the associated risks; and
    (g) there are sound audit procedures to ensure compliance with the insurer's policies and procedures and statutory requirements.

Asset-Liability Management

18. Asset-liability management ("ALM") allows decisions and actions taken with respect to assets and liabilities to be coordinated through the ongoing process of formulating, implementing, monitoring and revising strategies related to assets and liabilities in order to achieve an insurer's financial objectives, given its risk tolerance and other constraints. The insurer shall ensure that it has a Board-approved ALM policy which explicitly takes into consideration its investment management and product development and pricing functions. The ALM policy shall be appropriate to the nature, scale and complexity of the risks associated with the insurer's assets and liabilities.

19. An insurer shall ensure that its ALM policy:

    (a) recognises the interdependence between all of the insurer's assets and liabilities and take into account the correlation of risk between different asset classes as well as the correlation between different products and business lines, while recognising that correlations may not be linear; and
    (b) takes into account any off-balance sheet exposures that the insurer may have and the contingency that risks transferred may revert to the insurer.

20. Where relevant, the ALM policy shall include the following:

    (a) how the investment and liability strategies adopted by the insurer allow for interaction between assets and liabilities;
    (b) how the liability cash flows are met by the cash inflows; and
    (c) how the economic valuation of assets and liabilities are changed under an appropriate range of different scenarios.

Permitted Derivatives Activities

21. In view of the potential significant financial losses that could arise from speculative trades, an insurer shall, subject to paragraph 28 only carry out investments when it is capable of assessing the nature, scale and complexity of the risks associated with those investments.

22. An insurer shall only be permitted to enter into or effect derivative transactions for the purposes of hedging or efficient portfolio management.

23. An insurer shall disclose in its annual statutory returns, its accounting policies as well as exposure to derivatives (including the amount and percentage of derivatives of the total assets of the insurance fund and the shareholders' fund for each fund separately).

Hedging

24. An insurer shall clearly identify any derivative transaction entered into for hedging purposes as such. The insurer shall promptly unwind the transaction if the transaction does not have the effect of hedging at any stage during the period of the derivative contract.

25. An insurer shall exercise extra caution whilst hedging foreign currency risk where the underlying investment does not have a fixed payment schedule (e.g. equities).

Efficient Portfolio Management

26. For the purposes of this notice, a derivative transaction is effected for the purpose of efficient portfolio management if:

    (a) it is economically appropriate;
    (b) the exposure is fully covered (to meet any obligation to pay or deliver); and
    (c) it has at least one of the following aims:

        (i) reduction of risk;
        (ii) reduction of cost with no increase in risk or a minimal increase in risk; or
        (iii) generation of additional economic capital or income for the fund with no increase or a minimal increase in risk.

27. In determining if the transaction is economically appropriate, the insurer should have a reasonable belief that where it is undertaken to:

    (a) reduce risk or cost or both, it would diminish a risk or cost which is sensible to reduce; or

(b) increase economic capital or generate income for the relevant insurance fund or shareholders' fund, the fund would (barring events which are not reasonably foreseeable) derive a benefit from the transaction.

Prohibitions

28. An insurer shall not take uncovered positions in derivatives. The insurer shall cover a derivative transaction which gives rise, or may give rise, to future commitments as follows:

    (a) in the case of derivative transaction which will, or may at the option of the insurer, be cash settled, the insurer shall hold, at all times, liquid assets sufficient to cover the exposure; or

    (b) in the case of derivative transactions which will, or may at the option of the counterparty, require physical delivery of the underlying assets, the insurer shall hold the underlying assets in sufficient quantities to meet the delivery obligation at all times. If the insurer deems the underlying assets to be sufficiently liquid, the insurer may hold as coverage other liquid assets in sufficient quantities, provided that such alternative assets may be readily converted into the underlying asset at any time to meet the delivery obligation.

Contravention of requirements imposed

29. Contravention of any requirement imposed under this Notice shall be an offence and shall attract the penalty specified in section 55(2) of the Act.

Effective Date

30. This Notice shall take effect on 1 January 2014.

Appendix A

Main Elements Of Board-Approved Written Investment Policy Of An Insurer

The main elements shall include the following:

1 Determination of the strategic asset allocation for each of the major product line or aggregated product lines, as may be appropriate, that is, the long-term asset mix over the main investment categories. This shall be done with due regard to asset-liability management[1], overall risk tolerance[2], long-term risk-return requirements and solvency position of the insurer.

2 Establishment of limits for the allocation of assets by geographical area, markets, sectors, counterparties and currency. In establishing the limits, the insurer shall ensure adequate diversification within a risk category and between different risk categories. Diversification within a risk category occurs where risks of the same type are pooled (e.g. shares relating to different companies). Diversification between risk categories is achieved through pooling different types of risk (e.g when two asset portfolios whose performances are not fully correlated are combined, the exposure to the aggregated risks will generally be lower than the sum of the exposures to the risks in the individual portfolios).

3 Formulation of an overall policy on the selection of individual securities and other investment titles. The insurer shall ensure that the overall policy results in investments where the associated risks of the asset can be properly managed by the insurer, i.e. insurer can identify, measure, monitor, control and report those risks and appropriately take them into account in its own risk and solvency assessment. In particular, the insurer shall identify and analyse assets which are lacking in transparency, including those inherent to the investment structure. The insurer shall indentify and adequately cover potential obligations to make future payments under such assets

4 Adoption of passive or more active investment management[3] in relation to each level of decision-making.

[1] The insurer shall specifically consider investment guarantees and embedded options that are contained in its policies, and the currency or currencies of its liabilities and the extent to which they are matched by the currencies of the assets.

[2] Various types of risks should be considered, including but not limited to, risk of counterparty default, deterioration in value (including currency risk).

[3] Passive management refers to the situation where investment transactions are undertaken in order to maintain a predefined strategic mix between asset categories, or within an asset category, possibly in accordance with market indices. Active management, on the other hand, refers to the situation where transactions are undertaken in order to deliberately deviate from the predefined strategic mix to achieve a risk-return profile different from that implied by the strategic portfolio composition. This may take place at various levels, for example by changing the portfolio mix between equities and fixed income investment; altering the geographical allocation; or, in an equity portfolio, over- and underweighting of shares against an index; and, in a fixed income portfolio, increasing or decreasing the duration of the portfolio.

5 In the case of active management, definition of the scope for investment flexibility, usually through the setting of quantitative asset exposure limits.

6 The extent to which the holding of some types of assets is ruled out or restricted where, for example, the disposal of the asset could be difficult due to the lack of liquidity of the market or where independent (i.e. external) verification of pricing is not available, and the levels at which such investments shall be held by the insurer.

7 Maintain proper books of account relating to each insurance fund and shareholders' fund and establish the framework of accountability for all asset transactions; these have to be audited at least yearly.

8 Policy for safe-keeping of assets, including custodial arrangements and the conditions under which investments may be pledged or lent.

9 Formulation of an appropriate risk management policy in respect of the investment activities of the insurer.