

# Prudential Standard FSB 1

## Framework for Financial Soundness of Branches

### ***Objectives and Key Requirements of this Prudential Standard***

*This Standard sets out the high-level framework for assessing the financial soundness of branches of foreign reinsurers in South Africa from a regulatory perspective. The principles set out in this Standard are supported by other specialised Standards and Attachments that address particular aspects of the framework (collectively the Financial Soundness Standards for Branches). These other Standards contain the technical details of the computations and requirements involved.*

*It is the responsibility of the foreign reinsurer and the representative of a branch to ensure that the branch meets the financial soundness requirements on a continuous basis.*

*The Financial Soundness Standards for Branches are designed to ensure that foreign reinsurers hold security in South Africa of sufficient quality and quantity to provide assurance, in combination with the foreign reinsurer's regulatory capital requirements in its home jurisdiction, that policyholder obligations will be met as they fall due and that the foreign reinsurer is able to absorb significant unforeseen losses arising from the risks associated with its insurance activities in South Africa.*

*The Financial Soundness Standards for Branches address the two related matters of assessing the value of technical provisions that a branch is required to hold as security in a trust and the valuation and limitations on the assets held in the trust.*

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### **1. Application**

- 1.1. This Standard applies to all branches of foreign reinsurers licensed under the Insurance Act, 2017 (the Act).

- 1.2. Unless otherwise indicated, all references to “insurer” in any other Standard referred to in this Standard can be read as a reference to a branch of a foreign reinsurer.

## **2. Roles and Responsibilities**

- 2.1. Ultimate responsibility for the prudent management of the financial soundness of a branch of a foreign reinsurer rests not with the Prudential Authority but with the foreign reinsurer and the representative of a branch.
- 2.2. The representative of a branch must have in place procedures to monitor that the branch meets its regulatory requirements at all times. The representative must without delay alert the Prudential Authority of any circumstances that could lead to a breach of the regulatory requirements within the following three months.
- 2.3. The representative of a branch must ensure that, where approvals are required from the Prudential Authority, those approvals have been obtained.
- 2.4. A branch’s head of actuarial function is responsible for expressing an opinion to the representative regarding the accuracy of the calculations and the appropriateness of the assumptions underlying the valuation of the branch’s technical provisions.
- 2.5. A branch’s auditor must audit the financial soundness of a branch in accordance with its legal and regulatory obligations. The auditor must report to the foreign reinsurer, the representative and Prudential Authority any matters identified during the performance of its responsibilities that may cause the branch not to meet its regulatory requirements.
- 2.6. The roles and responsibilities of the representative of a branch and the head of actuarial function are described in more detail in the Governance and Operational Standards for Branches (GOB 1).

## **3. Commencement and Transition Provisions**

- 3.1. This Standard commences on 1 July 2018.

<b>Version Number</b>	<b>Commencement Date</b>
1	1 July 2018

## **4. Framework for Financial Soundness of Branches**

- 4.1. The framework for financial soundness of branches consists of the following elements:
- a) Branches must hold, in trust, an amount at least equal to the value of its technical provisions less the value of premium debtors as security for its insurance obligations stemming from insurance business written in South Africa;
  - b) In determining the amount to be held in the trust, both assets and liabilities must be valued on a basis consistent with market-based methodologies, unless otherwise specified; and

- c) The amount to be held in trust is subject to limitations on the type and spread of assets that may be held as trust assets.
- 4.2. The framework is built on a combination of requirements set out in the Financial Soundness Standards for Insurers (FSIs) and more specific requirements only applicable to branches. The specific requirements are set out in the Financial Soundness Standards for Branches (FSBs) and reference is made to the FSIs where applicable.

## **5. Assessing Financial Soundness of Branches**

- 5.1. Branches are required to monitor and assess their financial soundness on an ongoing basis. A branch is required to value its technical provisions and assets on at least a quarterly basis or when a material change to the risk profile can have a material impact on the technical provisions. The results of this valuation must be reported to the Prudential Authority in line with timeframes required for financial reporting purposes.
- 5.2. Branches must also value and report their technical provisions and assets when otherwise requested to do so by the Prudential Authority.
- 5.3. A branch must ensure, within the timeframe provided in section 6.4 below, that the value of the assets held in the trust are at least equal to the value of its technical provisions less the value of premium debtors as at the end of the most recent quarter, or as at the point in time that either the Prudential Authority requested a valuation or there was a material change in the risk profile, whichever is the later date.

## **6. Adjusting Trust Assets**

- 6.1. Branches must hold trust assets, valued in accordance with FSB 2 (Valuation of, and limitations on, assets held as security by branches), at least equal to the value of its technical provisions less the value of premium debtors.<sup>1</sup>
- 6.2. The technical provisions must be valued in accordance with FSB 3 (Valuation of Technical Provisions by Branches).
- 6.3. Premium debtors can only be deducted if they are less than 120 days old and to the extent that they can be offset against future claims for each cedant separately.
- 6.4. Branches must adjust, within 45 days, trust assets so that the value of trust assets is at least equal to the value of technical provisions less the value of premium debtors calculated as at the relevant date as outlined in section 5.3 above.
- 6.5. The adjustments made to the trust assets for the first quarter of each financial year must also comply with any adjustment that may be necessary as a result of the external audit outcome in respect of the previous financial year.

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<sup>1</sup> Section 40(1) of the Act provides that the Prudential Authority may prescribe requirements in this regard.

## **7. Regulatory Intervention**

- 7.1. The financial soundness framework establishes a trigger point for regulatory intervention.<sup>2</sup> If the Prudential Authority is satisfied that a branch has failed or may, in the following three months, fail to provide or maintain the required security it may, in addition to directing the branch to rectify the actual or potential breach, suspend or withdraw the branch's licence.

## **8. Structure of the Financial Soundness Standards for Branches**

- 8.1. The Financial Soundness Standards for Branches are organised as follows:

FSB 1	Framework for Financial Soundness of Branches
FSB 2	Valuation of, and limitations on, assets held as security by Branches
FSB 3	Valuation of Technical Provisions by Branches

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<sup>2</sup> The Prudential Authority's powers to intervene in this respect are set out in section 42 of the Act.

## **Attachment 1: Definitions in the Financial Soundness Standards for Branches**

The terms used in the Financial Soundness Standards for Branches are defined in Attachment 1 of FSI 1 Framework for Financial Soundness of Insurers.

## **Attachment 2: Abbreviations**

Abbreviations used in the Financial Soundness Standards for Branches are defined in Attachment 2 of FSI 1 Framework for Financial Soundness of Insurers.