

**INSTRUCTION OF BCTL No. 07/ 2020
ON MINIMUM SOLVENCY AND ADMITTED ASSET REQUIREMENTS
FOR GENERAL INSURANCE COMPANIES**

Taking into consideration of the necessity for general insurance companies to adopt consistent prudential financial requirements and methodologies in order to measure their individual solvency margin requirements.

Furthermore, the need for general insurance companies to maintain total assets in their books that exceed their total liabilities as a buffer or a source of financial support to protect an insurer against unexpected losses, and is therefore, a key contributor to its safety and soundness.

It is crucial for insurance companies to be solvent at all times and be able to fulfil their contractual obligations to their policyholders and the insuring public under all reasonably foreseeable circumstances.

For the purpose of providing an early warning for regulatory intervention and early corrective action.

Considering also the article 27 of the Law no. 6/2005, of 7 of July, Law of Licensing, Supervision and Regulation of Insurance Companies and Insurance Intermediaries, that grants exclusive competence to the BCTL to regulate, by Instruction, the margin solvency requirements.

The Governing Board of Banco Central de Timor-Leste pursuant to the authority granted in Article 31 paragraph 1 of Law no. 5/2011 of 15 June, and in Law no. 6/2005, of 7 of July, hereby resolves to approve the following Instruction:

**Article 1
Definitions**

In this Instruction the terms below shall have the following meaning:

- (a) "Admitted assets" means the assets or class of assets specified herein and within the values specified herein;
- (b) "BCTL" means the Banco Central de Timor-Leste as established under Law no. 5/2011 of 15 June;
- (c) "Cash and deposits" mean cash, bank balances and deposits (including fixed deposits, negotiable instruments of deposit, bankers' acceptances and money market instruments) deposited by any financial institution licensed by the Central Bank;
- (d) "Equity Instrument" means any kind of financial asset representing ownership rights on a commercial company under Timor-Leste law;
- (e) "Group of borrowers" means a set of natural persons or corporate entities, as the case may be, which are:
 - (i) Related corporations or close relatives;
 - (ii) Associate companies and for the purpose of determining an "associate", the cut-off level is the ownership or control, directly or indirectly, of not less than 20% of the issued capital; or
 - (iii) In the position of a partner in a partnership or a "controller" or an institution controlled as defined under the relevant Law or Regulation applicable in Timor-Leste;
 - (iv) However, if a borrower is obtaining a credit facility for its own use and not for the use of other entities referred to above, and where the credit facility is extended to it on the basis of its own financial strength without recourse to

any other person within the group of borrowers, such a credit facility need not be aggregated with other credit facilities extended to the group.

- (f) "Low risk assets" means:
 - (i) A security, bill, certificate or loan or any other paper issued and guaranteed by the Government of Timor-Leste;
 - (ii) A security, bill, certificate or loan or any other paper issued by the BCTL; and
 - (iii) A US dollar denominated bond issued by a foreign sovereign with a sovereign rating from at least two major rating agencies of AA- or better.
- (g) "Property" includes "immovable property" and other "approved property-related investments" defined as follows:
 - (i) "immovable property" means self-occupied property or investment property;
 - (ii) "approved property-related investments" means private real-estate funds (fund), and shares of unlisted single-purpose property holding companies (entity) whose principal assets comprise of properties and which do not have significant liabilities other than in relation to loan facilities taken for the purchase of property, which meet the following conditions:
 - (a) the fund/entity shall be established or incorporated in Timor-Leste;
 - (b) investments in property shall be made in Timor-Leste property only;
 - (c) the fund/entity shall wholly own a property, including all rights, interests and benefits related to the ownership of the property;
 - (d) at least one of the main sponsors or managers of the fund should be a financial institution licensed by the Central Bank;
 - (e) in the case of an investment by a fund in the shares of a single-purpose property holding company, the company should not have significant liabilities other than in relation to loan facilities taken for the purchase of property and the valuation of the acquired company must be backed by the value of properties owned by the company.
- (h) "Unsecured credit facility" means a credit facility other than a secured facility and which carries a minimum rating of BBB by any recognized rating agency;
- (i) "Secured credit facility". A secured credit facility shall be secured in the manner set out under Article 5.

Article 2

Applicability

This Instruction shall apply to all general insurance companies licensed by BCTL.

Article 3

Required Minimum Capital

1. The capital of a general insurance company shall be calculated based on the company's balance sheet prepared according to internationally recognized accounting standards as the sum of the following:
 - (a) Issued and fully paid-up ordinary shares;
 - (b) share premiums;
 - (c) paid-up irredeemable preference shares;
 - (d) capital reserves;
 - (e) retained earnings (less losses); and
 - (f) revaluation reserves for self-occupied properties.

2. General insurance companies shall always maintain a minimum capital unimpaired by losses of at least US\$500,000.00 (five hundred thousand United States of America dollars).
3. In line with Article 10 (2) of Law No. 6/2005 of 7 July, the first US\$500,000.00 (five hundred thousand United States of America dollars) capital requirement at the time of establishment must be in the form of share capital.
4. The initial capital of a general insurance company shall be permanent in nature and subscribed in cash and shall not be provided by way of loan, bond or other debt instrument.
5. When the capital of a general insurance company falls below the required minimum capital, the shareholders of the company must subscribe further capital within a maximum period of 30 days so that the minimum capital requirement is met.

Article 4

The Principal Areas of Concern in Reviewing an Insurer's Investment Portfolio

1. Diversification: This is to ensure that the investment portfolio is adequately diversified to prevent an undue concentration of investment by type or issue.
2. Liquidity: This is to ensure that investment structure is appropriately liquid to allow for generating the necessary cash flows to pay liabilities when they come due.
3. Sufficient: Assets should be readily convertible to cash and the sale of necessary assets should not involve significant losses caused by market impact.
4. Quality: This is to ensure that the investments held are of good quality. As the quality of an investment decreases, the probability that the principal will be returned and that the expected yield will be realized, tends to decrease.
5. Valuation: This is to ensure that the investments have been appropriately valued in accordance with internationally recognized accounting standards.

Article 5

Prohibited Acts or Transactions

1. A general insurance company licensed shall not accept immovable property as security for a credit facility unless it is freehold property or leasehold property with at an unexpired lease period of at least 25 years.
2. A licensed insurer shall not grant a credit facility:
 - (a) for the purchase of immovable property for residential purpose, more than 80 percent of the purchase price; or
 - (b) for any other purpose, more than 70 per cent of the market value of the immovable property on the date of granting the credit facility.
3. A licensed general insurer is prohibited to provide following credit facilities for the following:
 - (a) loans granted to shareholders or partners, directors, managers or employees of the insurance company itself, or to the spouses of any such person, and
 - (b) loans granted to companies belonging to the same group in which the insurance company operates.

Article 6

Admitted Assets Supporting Total Liabilities and Margin of Solvency

1. A general insurer shall maintain admitted assets of a value not less than the required margin of solvency and its total liabilities.
2. A licensed general insurer shall maintain the limit for admitted assets as described on the **Annex II** of this Instruction.

3. Investment in unsecured credit facilities rated below BBB by international rating agencies are not qualified as admitted assets.

Article 7
Calculation of Required Margin of Solvency

1. A licensed general insurer shall maintain a margin of solvency (MOS) in respect of its general business which shall be the higher of all the following amounts:
 - (i) US\$500,000.00 (five hundred thousand United States of America dollars); or
 - (ii) 25% of net premiums; or
 - (iii) 25% of net claims incurred
2. General insurance companies must, at all times, maintain a margin of solvency not less than the minimum capital requirement.
3. Where an insurer registers an abnormal loss ratio during the preceding three consecutive years or during any three years of the preceding five years, the margin of solvency shall be double the amounts calculated in accordance with the table in paragraph 1.
4. Refer to **Appendix I** for **Statement of Solvency**.

Article 8
Failure to Meet Solvency Margin

1. General insurance companies that fail to meet the minimum capital requirement or the minimum solvency margin prescribed in this Instruction must notify the BCTL within one business day of the shortfall being identified by management.
2. Within one week of their notification to the BCTL, insurance companies in this position must submit a plan for addressing the deficiency that describes the manner in which the deficiency will be overcome, and the date (not being more than 60 days from the discovery of the shortfall) by which the deficiency will be cleared.
3. If the failure to meet the minimum capital/solvency margin persists beyond the clearance date the BCTL shall apply increasingly punitive sanctions at such intervals as it may deem appropriate to protect the interests of the policyholders and creditors of the general insurance company in line with Law No. 6/2005 of 7 July.

Article 9
Entry into force and Publication

This Instruction shall enter into force on the day of its publication in the Jornal da República.

Adopted on 28 August 2020

Governor

Abraão de Vasconcelos

Annex I Statement of Solvency

Statement of Solvency

Name of Insurer: _____

As at: _____

No.	Items	Value US\$
1.	Total Admitted Assets (a)	
2.	Total Liabilities as per the company Balance Sheet (b)	
3.	Available Margin of Solvency (a-b) = (c)	
3.	Required Margin of Solvency (d) (The higher of US\$500,00.00 (five hundred thousand United States of America dollars) or computed amount	
4.	Solvency Surplus/ (Deficit) = (c-d)	
5.	Solvency Margin Ratio (SMR)* = (c/d)%	

* An insurer is required to maintain SMR of not less than 100% at all times.

Name and Signature of Managing Director: _____

Date: _____

Note: Please note that the statement of solvency should be filed together with the quarterly returns.

Annex 2: Limits for Admitted Assets

No.	Class of Assets	Limit for aggregate investments in a particular asset class	Sub-limit for individual Investments/exposures to individual counter-parties
1.	Low risk asset	No limit	No sub-limit
2.	Cash and deposits issued by institutions licensed by the central bank	No limit	No sub-limit
3.	Properties (a) Immovable properties (b) Other approved property-related investment	20%*	The lower of- a. 5% of (MOS + TL**); or b. 5% of the total issue of the fund, or the investee company's equity at the date of investment.
4.	Secured credit facilities	30%*	5% of the (MOS + TL) for total secured credit facilities to any one borrower or group of borrowers.
5.	Equity instruments (Excluding the capital or stock of a company of the same economic group)	20%*	The lower of- (a) 5% of (MOS+TL); or (b) 5% of investee company's equity.
6.	American dollar denominated mutual fund schemes	10%*	The lower of – (a) 5% of (MOS+TL); or (b) 5% of the total issue of the mutual fund at the date of investment.
7.	Other Assets:		
	(a) Reinsurance deposits with ceding companies which are not yet due for repayment	20%*	No sub-limit
	(b) Outstanding premiums other than motor business which are outstanding for not more than 60 days	20%*	No sub-limit
	(c) Claims recoverable and amounts due from reinsurers or ceding companies which are outstanding for not more than 3 months	No limit	No sub-limit
	(d) Investment income outstanding or accrued for not more than 3 months	No limit	No sub-limit
	(e) Cash proceeds from sale of assets which are outstanding not more than 15 days.	No limit	No sub-limit

* % of (MOS+TL)

** TL =Total Liabilities