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NATIONAL BANK OF ETHIOPIA

LICENSING AND SUPERVISION OF INSURANCE BUSINESS

INSURANCE RISK BASED CAPITAL
DIRECTIVE NO. SIB/--/2025

Whereas it is essential for the National Bank to receive relevant, reliable and timely financial and non-financial information to assess the financial soundness, managerial effectiveness and stability of each insurance company and the sector on an on-going basis;

Whereas the appropriate capital is important for the financial soundness of the insurance company, and ultimately for the protection of policyholders;

Whereas it is ultimately the responsibility of the Board and Senior Management to ensure that the insurance company maintains a capital adequacy level that is commensurate to their risk profile;

Now, therefore, in accordance Articles 23 and 64(2) of Proclamation No.746/2012 as amended by Insurance Business (Amended) Proclamation No. 1163/2019, the National Bank of Ethiopia hereby issues this Directive.

1. Short Title

This Directive may be cited as **The Insurance (Risk Based Capital) Directive No. SIB/--/2025.**

2. Definitions

In this directive, unless the context otherwise requires:

2.1 "**Minimum Capital Requirement**" means the level of capital below which an insurance company is regarded not viable to operate effectively;

2.2 "**Solvency Capital Requirement**" means the level of capital above which the Bank shall not intervene on capital adequacy grounds;

2.3 “**available capital**” means capital resources that qualify to meet the risk-based capital requirements;

2.4 “**capital resources**” mean financial instruments and other capital elements that provide loss absorbency on a going concern, in adverse circumstances and during a winding-up for the purposes of policyholder protection and financial stability;

2.5 “**capital adequacy**” means to the extent eligible capital resources is higher than the capital required under this directive;

2.6 “**counterparty**” means any person who is under a financial obligation to the insurance company;

2.7 “**equity**” means a share or any other form of ownership interest in a legal entity.

2.8 “**inadmissible asset**” means an asset of an insurance company, or a reinsurance company specified in this Directive that is required to be deducted from the total Tier 1 capital and eligible Tier 2 capital in accordance with requirements of the Directive;

2.9 **“Tier 1 Capital** “means highest quality, most loss absorbent and permanent form of capital;

2.10“**Tier 2 Capital**” means capital resources that possess characteristics of subordination to policyholders;

2.11 “**risk based capital**” means the aggregate of the capital required to address all relevant and material risks categories;

2.12“**eligible capital**” means qualifying capital resources that are capable to provide loss absorbency on a going concern, in adverse circumstances and during a winding-up for the purposes of policyholder protection and financial stability shall form the capital available;

2.13**“eligible own funds”** means actual own funds that are eligible to qualify for the coverage of the Solvency Capital Requirement (SCR) and Minimum Capital Requirement (MCR).

2.14 “**fair value reserve**” means unrealized gains/losses resulted from the valuation of available-for-sale and held for trading financial assets based on current market prices;

2.15“**subordination**” means degree to which and in what circumstances the capital element is subordinated to the rights of policyholders and non-subordinated creditors in during the winding up, insolvency, bankruptcy and liquidation of the insurance company;

2.16“**availability**” means level to which the capital element is fully paid and available to absorb losses;

2.17“**loss absorbing capacity**” means the extent to which the capital element absorbs losses;

2.18 “**permanence**” refers the period for which the capital element is available for the insurance company; and

2.19“**encumbrance**” means extent to which the capital element is attached to mandatory payments or service costs.

3. Scope of Application

This directive shall be applicable to all insurance companies and an Ethiopian reinsurance company operating in Ethiopia.

4. Minimum paid up capital

4.1 The minimum paid up capital prescribed for the purposes of this Directive is:-

a) in the case of a non-life insurance company, Birr 400 million;

b) in the case of a reinsurance company, Birr 500 million; and

c) in the case of a life insurance company, Birr 100 million.

4.2 An insurance company shall maintain at all times a Minimum Capital Requirement (MCR) which represents a CAR of 100%

4.3 An insurance company shall ensure that its eligible capital resources exceed the capital required at all times.

4.4 An insurance company shall maintain Solvency Capital Requirement (SCR) which represents a CAR of 150%.

5. Capital Available

5.1 The capital available to an insurance company shall be divided into two tiers based on the subordination, availability, loss absorbing capacity, permanence, and absence of encumbrances and/or mandatory servicing costs.

5.2 The Capital Available of an insurance company or a reinsurance company shall consist of the sum of its Tier 1 Capital and its eligible Tier 2 Capital less the sum of the inadmissible assets.

5.3 The Tier 1 Capital of an insurance company shall be the highest quality, most loss absorbent and permanent form of capital.

5.4 The Tier 1 Capital of an insurance company shall be the sum of —

a) the issued and fully paid-up ordinary shares of the insurance company.
b) share premium.
c) legal reserves maintained by the insurance company; and
d) retained earnings by the insurance company

5.5 Tier 2 capital resources possess certain characteristics such as subordination to policyholders and non-subordinated creditors.

5.6 The Tier 2 capital shall consist of the following components—

a) Fair Value Reserves,
b) Insurance Finance Reserve
c) Other Reserves.

5.7 As far as compliance with the Solvency Capital Requirement is concerned, the eligible amounts of Tier 1 and Tier 2 items shall be subject to all of the following quantitative limits:

a) the eligible amount of Tier 1 items shall be at least one half of the Solvency Capital Requirement;
b) the eligible amounts of Tier 2 items shall not exceed 50 % of the Solvency Capital Requirement.

5.8 As far as compliance with the Minimum Capital Requirements is concerned, the eligible amounts of Tier 2 items shall be subject to all of the following quantitative limits:

a) the eligible amount of Tier 1 items shall be at least 80 % of the Minimum Capital Requirement;

b) the eligible amounts of Tier 2 items shall not exceed 20 % of the Minimum Capital Requirement.

5.9 For the purposes of determining the available capital of an insurance company or a reinsurance company, the following items shall be deducted from the sum of Tier 1 and eligible Tier 2 capital.

a) intangible assets, including goodwill, patents, software, trademarks.

b) prepaid expenses.

c) deferred tax assets, net of deferred tax liabilities, if any.

d) furniture, fixtures and fittings.

e) any asset that is subject to a mortgage, charge or any other encumbrance, including a pledge.

f) receivables, including due from reinsurance companies, past due one year

5.10 For the purpose of calculating a general insurance company's capital adequacy, the general insurance company shall apply the following concentration limit factors.

a) for deposits in any one financial institution or group of related companies, ten percent of total assets.

b) for shares of any one institution or group of companies, fifteen percent of total assets.

c) for property, twenty percent of the total assets; and

d) for investment in related parties, ten percent of total assets.

5.11 For the purpose of calculating a life insurance company's capital adequacy, the life insurance company shall apply the following concentration limit factors.

a) for deposits in any one financial institution or group of related companies, ten percent of total assets.

b) for shares of any one institution or group of companies, fifteen percent of total assets.

c) for property, thirty percent of total assets; and

d) for investment in related parties, ten percent of total assets

6. Capital Required

6.1 The capital required of an insurance company shall be determined based on the risk profile of the company.

6.2 The capital requirement applicable to a licensed insurance company shall be the greater of—

a) an amount equal to its minimum paid up capital requirement, as specified in regulation 3.1.

b) its risk-based capital requirement calculated in accordance with regulation 5.3.

6.3 The risk-based capital requirement of an insurance company shall include capital for the insurance risk, market risk, credit risk and operational risk.

6.4 The risk-based capital requirement shall be calculated in accordance with the following formula:

$$\textbf{Risk Based Capital} = \sqrt{(\textbf{Insurance Risk Capital})^2 + (\textbf{Market Risk Capital})^2 + (\textbf{Credit Risk Capital})^2} + \textbf{Operational Risk Capital}$$

7. Insurance Risk Capital Requirements

7.1 The insurance risk capital (IRC) shall be required to provide for the purpose of cushioning an insurance company or reinsurance company against unexpected changes in the level and trend to the value of technical provisions.

7.2 The required capital for non-life insurance company or reinsurance company shall include capital against fluctuations in the premium reserves, claim reserves and catastrophic risk.

7.3 For the purpose of the non-life insurance company or non-life re-insurance company, insurance liabilities shall be classified by the class of business.

7.4 The insurance risk capital requirement for non-life insurance company shall be the sum of

a) the premium reserves capital calculated as the sum of net unearned premium provision and premium deficiency provision risk multiplied by capital charge for each class of business.

b) the claim reserves capital calculated as the sum of net outstanding claims, net provision for claims incurred but not reported and net provision for claims incurred but not enough multiplied by capital charge for each class of business.

c)the catastrophic risk capital calculated as the net technical provisions multiplied by capital charge for catastrophic risk.

7.5 An insurance company shall, for the purpose of calculating the capital required for insurance risk, use the capital charges set out in Schedule 1(a).

7.6 An insurance company writing life business shall, where applicable, hold capital against adverse experiences resulting from mortality, longevity, morbidity, disability, expenses, lapses and catastrophes.

7.7 A life insurance company shall calculate the insurance risk capital by using the capital charge on the actuarial liability value per class of life insurance business

7.8 The life insurance company shall be required to use the capital charges in Schedule 1(b).

8. Market Risk Capital Requirements

8.1 The capital required by an insurance company for market risk shall be for the purpose of cushioning against volatility in the market prices of assets held by the insurance company used to back policyholder liabilities.

8.2 The market risk capital for an insurance company shall be the sum of the following—

a) the capital requirement for equity risk calculated as the market value of equities multiplied by the capital charge as provided for in Schedule 2a.

b) the capital requirement for property risk calculated as the market value of property multiplied by the capital charge as provided for in Schedule 2a; and

c) the capital requirement for foreign currency risk calculated as the net balance sheet positions for exposures to each of the different currencies converted into Ethiopian Birr at the spot exchange rates at the valuation date as provided for in Schedule 2a.

d) the capital requirement for interest rate risk calculated as base yield curve multiplied by (1 + stress-up), and (1 — stress-down) for the increasing and decreasing scenarios respectively as provided for in Schedule 2b.

8.3 An insurance company shall, for the purposes of calculating the capital required for market risk, apply a capital charge to the balance sheet asset value

9. Credit Risk Capital Requirements

9.1 The capital required for credit risk aims to cushion against risk of losses resulting from counterparty default.

9.2 An insurance company shall calculate a reinsurance risk capital charge for each reinsurance counterparty based on the credit rating.

9.3 The credit risk for counterparty shall be calculated as the total credit exposure multiplied with the capital charge as provided for in Schedule 3.

10. Operational Risk Capital Requirements

10.1 The operational risk capital for an insurance company shall be used to cushion against losses that may arise from failed processes, systems and people.

10.2 The operational risk capital shall be computed as thirty percent of the square root of the sum of the squares of the capital required for insurance risk, market risk and credit risk.

Operational Risk Capital =

$$30\%*\sqrt{(\textbf{Insurance Risk Capital})^2 + (\textbf{Market Risk Capital})^2 + (\textbf{Credit Risk Capital})^2}$$

11. Enforcement

11.1 Where the National Bank determines non-compliance with the provisions of this Directive, it may take any intervention prescribed in the Proclamation.

11.2 The National Bank shall implement the following statutory actions based on the insurance companies CAR position.

CAR range	Regulatory Implication
CAR>150%	The insurer is not subjected to intervention measures where it has been determined that it has a sound financial position.
CAR Between 125% and 150%	The insurer is required to submit an acceptable recovery plan to improve its capital position.
CAR Between 110% and 125%	The insurer board is required to submit a commitment to implement the recovery plan within a specified timeframe.
CAR Between 100% and 110%	The regulator takes over control of an insurance company (Statutory Management). The regulator will appoint administrators
CAR less 100%	The supervisor revoke the insurer's license and initiate a wound up process

12. Reporting Requirements

12.1 An insurance company or reinsurance company shall calculate its capital adequacy ratio—

a) within 90 days of the last day of each financial year;

b) within 30 days of the last day of the first, second and third quarters of each financial year;

c) on the occurrence of any adverse event that may affect the on-going solvency of the insurance company or reinsurance company; and

d) if required to do so by the National Bank.

12.2 An insurance company or reinsurance company shall be required to submit the CAR using the template provided by the National Bank.

12.3 Non-compliance with the reporting requirements and within the set deadlines is punishable with the administrative and pecuniary sanctions provided for in relevant regulations and directives

12.4 Where the National Bank determines non-compliance with the provisions of this Directive, it may take any intervention prescribed in the Proclamation.

13. Schedules

Schedule 1 (a) — Insurance Risk — Non-Life

Class of Business	Premium Reserve— Risk Charge	Claims Reserve— Risk Charge
Aviation Insurance	37.00%	29.00%
Engineering Insurance	10.00%	8.00%
Marine Insurance	11.00%	9.00%
Energy Insurance	10.00%	8.00%
Liability Insurance	18.00%	14.00%
Motor Insurance	11.00%	9.00%
Personal Accident	15.00%	12.00%
Workmen's Compensation	18.00%	15.00%
Health and Medical	11.00%	9.00%
Theft Insurance	25.00%	20.00%
Fire Insurance	10.00%	8.00%
Agricultural Insurance	9.00%	7.00%
Bond Insurance	27.00%	21.00%
Miscellaneous Insurance	13.00%	10.00%
Catastrophic Risk	2.00%	2.00%

Schedule 1 (b) — Insurance Risk - Life

Class of Business	Capital Charge
Life Assurances	4.50%
Annuities	3.00%
Personal Pensions	3.00%
Permanent Health	3.50%
Linked Investment	1.50%
Non-Linked Investments	1.50%
Deposit Administration	1.50%
Group Life	8.00%
Group Credit	10.00%
Other Life Insurance	5.00%

Schedule 2a — Market Risk

Type	Asset	Capital Charge
Equity Risk	Shares in Listed Companies	25.00%
	Shares in Unlisted Companies	35.00%
Property Risk		
	Investment Property	20.00%
	Owner Occupied Property	25.00%
	Leasehold Property	25.00%
Foreign Currency Risk		
	USD	4.50%
	Euro/Pound	6.00%
	Other Foreign Currency	8.00%

Schedule 2b — Interest Rate Risk Capital

Scenario	Value of Assets	Value of Liabilities	Surplus
Base scenario — assets and liabilities valued as for risk-based balance sheet	A0	L0	S0=A0-L0
Up shock — assets and liabilities valued assuming market interest rates increase by 1.5%	A1	L1	S1=A1-L1
Down shock — assets and liabilities valued assuming market interest rates decrease by 1.5%	A2	L2	S2=A2-L2
Interest Rate Risk Capital			MAX((S0-S1), (S0-S2),0)

Schedule 3- Credit Risk

Asset Type	Capital Charge
Government Securities	0.00%
Corporate Bonds	12.00%
Commercial Paper	12.00%
Term Deposits	0.00%
Cash and Cash Equivalents	0.00%
Outstanding Premiums	
Less than 30days	30.00%
More than 30days	100.00%
Receivables from unrelated parties	
Less than 30days	10.00%
More than 30days but less than 90days	25.00%
More than 90 days	100.00%
Receivables from related parties	40.00%

Reinsurance Share/Recoveries and Receivables	
Reinsurance companies rated AA or Higher	1.60%
Local Regulated Reinsurance company	1.00%
Reinsurance companies rated A	4.00%
Reinsurance companies rated BBB	8.00%
Reinsurance companies rated BB	10.00%
Reinsurance companies rated B or Below	25.00%
Unrated	100.00%
Loans	
Loans to Employees	30.00%
Policy Loans	20.00%

14: Effective Date:

This Directive shall enter in to force as of the day of … 2025.