Directive No. SIB/24/2004

LICENSING AND SUPERVISION OF INSURANCE BUSINESS
Amendment of
PROHIBITION OF ISSUANCE OF CERTIAN TYPES OF BONDS BY INSURANCE COMPANIES

Whereas insurance companies in Ethiopia offer Financial guarantee Bonds and other Unconditional Bonds as one of their products to cover losses that may arise as a result of failure of an obligor to settle in full financial obligations;

Whereas the basis on which such bonds are issued (physical collateral or financial standing of the borrower) are not well suited to insurers to serve them as adequate safe guards against losses;

Whereas there is no reliable and readily available reinsurance arrangement for such bonds;

Now, therefore, in order to prevent possible losses that insurers may suffer as a result of issuing Financial Guarantee Bonds and other Unconditional Bonds, the National Bank of Ethiopia has issued the following directives in line with the powers vested in it by Article 42 (j) of the Licensing and Supervision of Insurance Business Proclamation No. 86/1994.

1. Definitions

For the purpose of these directives:

"Bank" shall mean the National Bank of Ethiopia;

"Aggregate Exposure" shall mean the maximum potential financial liability of an insurance company to beneficiaries arising from the issuance of Financial Guarantee Bonds and Unconditional Bonds by the insurance company;

"Financial Guarantee Bond" shall mean a bond payable on demand issued by an insurance company obliging such insurance company to pay to a lending bank or another creditor or supplier all outstanding claims arising from non-payment by principal debtor or debtors;

"Unconditional Bond" shall mean a bond other than Financial Guarantee Bond issued by an insurance company that is payable to the beneficiary on demand, without any pre-conditions attached to such payment.

Prohibition

Insurance companies are prohibited from issuing a Financial Guarantee Bond, by whatever name it may be referred to, in any form whatsoever;

Insurance Companies are prohibited from issuing any Unconditional Bond, by whatever name it may be referred to.

3. Treatment of Financial Guarantee Bonds and Unconditional Bonds Issued and Outstanding Before the effective Date of these Directives

Financial Guarantee Bonds or Unconditional Bonds issued by insurance companies and outstanding as of the effective date of these directives shall be withdrawn upon expiry or shall be phased out by December 31, 2005;

Notwithstanding what is stated under 3.1 herein above, Financial Guarantee Bonds or Unconditional Bonds whose originally set expiry dates extend beyond December 31, 2005 as of the effective date of these directives shall be withdrawn upon expiry;

Insurance companies shall hold minimum provisions for Financial Guarantee Bonds and/or Unconditional Bonds in the following manner:

All premiums written on Financial Guarantee Bonds and/or Unconditional Bonds outstanding as of the end of February 2004 shall be kept as provisions for such bonds until the phase out period for such bonds specified under 3.1 and 3.2 herein above;

All premiums that may be written as a result of renewal of Financial Guarantee Bonds and//or Unconditional Bonds between the period end February 2004 and end-September 2005 shall form part of the provisions set out under (a) of this sub-article and shall be kept as provisions until the phase out period for Financial Guarantee Bonds and Unconditional Bonds specified under 3.1 herein above;

In addition to the provisions stated under (a) and (b) of this sub-article, insurance companies shall hold, effective end-June 2004, 5% of their aggregate exposure as provisions until the phase out period specified under 3.1 and 3.2 herein above:

4. Reporting Requirements

Insurance companies shall submit to the supervision Department of the Bank a quarterly Report, prepared in the manner as shown in the table attached to these directives.

5. Repeal

Directive No. SIB/23/2002 is hereby repealed and replaced by these directives.

Effective Date

These directives shall come into force as of the 1st day of March 2004