

የኢትዮጵያ ብሔራዊ ባንክ
NATIONAL BANK OF ETHIOPIA
አዲስ አበባ / ADDIS ABABA

LICENSING AND SUPERVISION OF REINSURANCE BUSINESS

Prudential Requirements for Reinsurance Companies Directive No. SRB/2/2022

Whereas, maintaining solvency of reinsurance companies is critically important for the maintenance of primary insurance companies' solvency and consequently it becomes necessary to require reinsurance companies to comply with financial reporting and regulation;

Whereas, it is necessary to ensure that licensed reinsurance companies are financially and operationally sound;

Whereas, inappropriate and inadequate retrocession arrangements could expose reinsurance companies to risks including insecurity, operational, legal, liquidity, and the combination of these and other risks which may affect the reinsurance company's financial soundness and reputation, and ultimately contribute to their failure;

Whereas, setting standards to reinsurance companies with regard to operation and documentation of underwriting, claims management, selection of retrocessionaires, designing of retrocession programs and implementation; review, monitoring and control of the entire operations; and transparent reporting-of risk transfer programs is essential;

Now, therefore, the National Bank of Ethiopia has issued this Directive pursuant to the authority vested in it by Articles 5(8), 55 and 64(2) of the Insurance Business Proclamation No. 746/2012 as amended by the Insurance Business (Amendment) Proclamation No.1163/2019.

1. Short Title

This Directive may be cited as “**Prudential Requirements for Reinsurance Companies Directive No. SRB/2/2022**”.

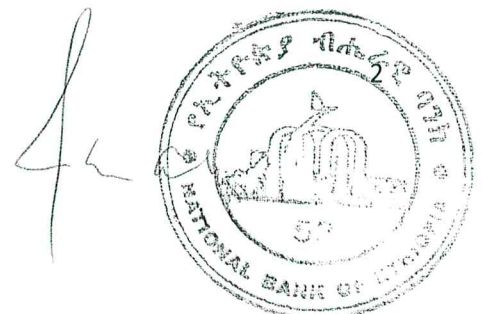
Handwritten signature



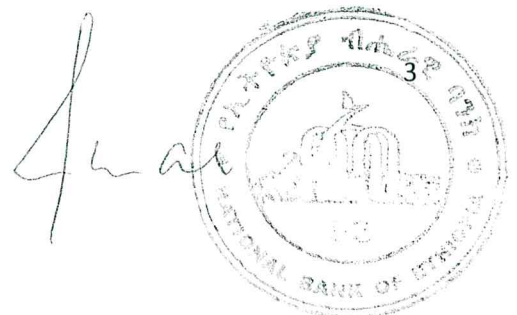
2. Definitions

For the purpose of this Directive, unless the context provides otherwise:

- 2.1. **“admitted capital”** means the difference between admitted assets and admitted liabilities;
- 2.2. **“admitted current assets”** means all assets reasonably expected to be sold, consumed or exhausted through the normal operations of a reinsurance company within the fiscal year but excluding non-admitted assets under sub-article 2.36 of this Directive;
- 2.3. **“admitted current liabilities”** means all liabilities of a reinsurance company that are expected to be settled in cash within the fiscal year including adjustments on it on legitimate grounds of accounting and insurance principles, laws and regulatory requirements;
- 2.4. **“admitted liabilities”** means all liabilities, as reported in the balance sheet including adjustment on it on legitimate grounds of actuarial, accounting, and insurance principles, laws and regulatory requirements;
- 2.5. **“board”** means the board of directors of a reinsurance company;
- 2.6. **“ceding company”** means an insurance or reinsurance company that cedes part of the insurance or reinsurance it has accepted from an insured to a reinsurance company;
- 2.7. **“cession”** means that portion of risk which the ceding company transfers to the reinsurance company;
- 2.8. **“cover note”** means a document between the reinsured and the reinsurance broker in which the broker informs the reinsured (its client) of the cover that has been obtained and hence the performance by the broker toward discharging its contractual duty of obtaining a cover;
- 2.9. **“credit rating”** means evaluation of credit worthiness or financial strength of a reinsurance company by A.M. Best, Fitch, Moody's, Standard & Poor's or any other such credit rating agencies acceptable to the National Bank;
- 2.10. **“due diligence”** means research, analysis and assessment of a reinsurance company prior to entering into a reinsurance or retrocession agreement;



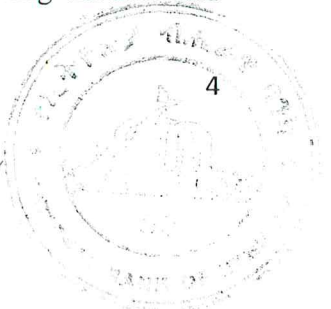
- 2.11. **“due from (re)insurance companies”** means receivables from (re)insurance companies arising from reinsurance contracts;
- 2.12. **“due to (re)insurance companies”** means payables to (re)insurance companies arising from reinsurance contracts;
- 2.13. **“eighths method(1/8th)”** means a basis of estimating unearned premium reserve, based on the assumption that annual policies are written evenly over each quarter and risk is spread evenly over the year or a method of premium reserving that is based on a quarterly accounting frequency;
- 2.14. **“expected maximum loss (EML)”** means the value of the largest expected loss that could result from an event, assuming the normal functioning of protective features and proper functioning of most (perhaps not all) active suppression systems such as firefighting appliances;
- 2.15. **“exposure”** means sum insured or the amount of the maximum monetary loss that a reinsurance company is liable to pay in respect of a particular risk or series of risks arising out of the occurrence of a certain specified event or events;
- 2.16. **“exposure retention”** means part of the sum insured a reinsurance company retains for its own net account from a single risk;
- 2.17. **“facultative retrocession”** means a type of retrocession that gives coverage for exposure(s) of individual risks that fall outside the automatic treaty capacity, scope and risk appetite of a reinsurance company. Facultative retrocession is negotiated separately and a reinsurance company retains the option to accept or decline each individual risk offered;
- 2.18. **“financial year”** means the financial year of a reinsurance company running from July 1st of any one year to June 30th of the following year;
- 2.19. **“fronting”** means an arrangement whereby a reinsurance company accepting a risk with the intent of ceding all or most of the exposure or assuming an exposure less than its retention capacity on a given risk;
- 2.20. **“general insurance business”** means all classes of business other than long-term reinsurance business;
- 2.21. **“investment property (real estate)”** means buildings constructed or acquired exclusively, or predominantly, for the purpose of generating income or for capital



appreciation and land acquired exclusively or predominantly for construction or development of facilities for the purpose of directly generating income.

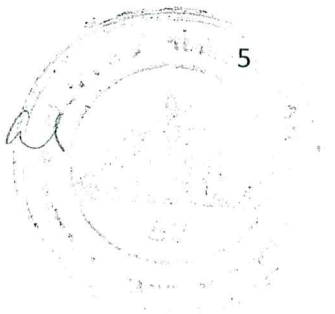
- 2.22. **“large or catastrophic exposure”** means one or more related risks, under the reinsurance contract, the consequences of loss of which could be disastrous;
- 2.23. **“legal reserve”** means part of net profit a reinsurance company is legally required to retain to its account;
- 2.24. **“ long-term insurance business”** means
- a. life insurance,
 - b. annuity,
 - c. pension,
 - d. permanent health insurance,
 - e. personal accident or sickness insurance underwritten by the insurance company incidental to any of the business as referred to (a) to (d) hereinabove, and
 - f. any other class of business as determined by the National Bank;
- 2.25. **“margin of solvency“** means the excess of admitted assets over admitted liabilities to be maintained by a reinsurance company;
- 2.26. **“National Bank”** means the National Bank of Ethiopia;
- 2.27. **“non-proportional treaty”** means a type of reinsurance where the allocation of liabilities between the cedant and the reinsurance company is based on claims and not on the sum insured. The reinsurance company accordingly undertakes to indemnify the cedant when the amount of claims exceeds a previously agreed amount (the deductible) and up to a maximum limit (the limit of cover);
- 2.28. **“person”** means a natural or juridical person;
- 2.29. **“proportional treaty”** means a type of reinsurance treaty whereby the primary insurance company and the reinsurance company share liabilities (sums insured), premiums and claims in a clearly defined proportion as described within the underlying treaty;
- 2.30. **“reinsurance”** means an agreement whereby a person provides insurance to a risk assumed by an insurance company;
- 2.31. **“reinsurance broker”** means a person that works for the ceding insurer and

Final



- reinsurance company to place its risks with another reinsurance company(s);
- 2.32. **“reinsurance company”** means a person that provides protection through the sale of reinsurance contracts;
- 2.33. **“retrocession”** means the process in which a reinsurance company transfers risks it has reinsured to another reinsurance company;
- 2.34. **“retrocessionaire”** means the assuming reinsurance company in a retrocession, where the ceding reinsurance company is known as the retrocedant;
- 2.35. **“slip”** means a paper document or an electronic message on which a reinsurance company confirms the amount of the risk that it is prepared to underwrite, together, generally, with a summary of the terms and conditions of the reinsurance contract pending the final wording is agreed and signed;
- 2.36. **“total assets”** means any property, security, item or interest of a reinsurance company recorded in its financial statement but excluding:
- 2.36.1. an asset that is pledged or mortgaged or charged for the benefit of a person other than the reinsurance company to the extent that it is so mortgaged,
 - 2.36.2. deferred and prepaid expenses,
 - 2.36.3. furniture, fixtures, dead stocks, stationeries... etc,
 - 2.36.4. due from reinsurance companies and ceding companies outstanding for more than one year,
 - 2.36.5. preliminary expenses incurred during the formation of the company,
 - 2.36.6. unsecured or inadequately secured loans and sundry receivables,
 - 2.36.7. computer software, goodwill and other intangible assets,
 - 2.36.8. any assets, with an unrealizable character,
 - 2.36.9. assets in excess of limits prescribed under sub-article 5.1.6 of this Directive, and
 - 2.36.10. any other asset the National Bank may consider unrealizable, inadequately secured;
- 2.37. **“treaty retrocession”** means an obligatory retrocession arrangement, usually for one year in cases of non-proportional and in continuous mode in the case of proportional treaties subject to prior notice of cancellation, which stipulates the

42



technical particulars and financial terms applicable to the reinsurance of some class or classes of business; and

- 2.38. any expression in the masculine gender includes the feminine and/or legal persons.

3. Scope of Application

The provisions of this Directive shall be applicable to all reinsurance companies licensed under Insurance Business Proclamation No. 746/2012 as amended by Insurance Business (Amendment) Proclamation No. 1163/2019 and Reinsurance Company Establishment Directive No. SRB/1/2014.

4. General Requirements

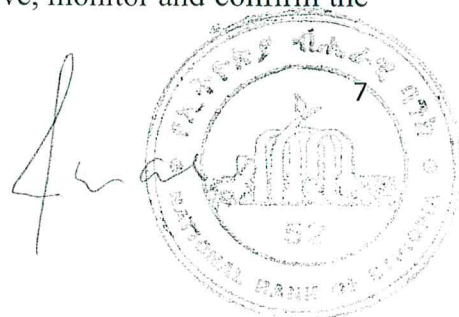
A reinsurance company shall:

- 4.1 have a sound retrocession program that at a minimum sets out:
 - 4.1.1 purpose and objectives of seeking retrocession and risk diversification,
 - 4.1.2 types of retrocession appropriate to each class of business; policy terms and conditions; cession and retention per risk, by line of business and aggregate exposure for the whole company,
 - 4.1.3 liquidity requirements taking into account possible mismatch between the payment of claims and the receipt of reinsurance recoveries,
 - 4.1.4 appetite for credit risk,
 - 4.1.5 selection of retrocessionaires including how to assess their security, automatic underwriting capacity, sufficient scope and continuity,
 - 4.1.6 criteria for providing and acquiring facultative covers,
 - 4.1.7 transaction tracking system, management, reporting and internal control of the overall retrocession operations,
 - 4.1.8 scope of authority and specification of matters reserved for the Board and management, and
 - 4.1.9 limits on the amount and type of reinsurance that will be



automatically covered by treaty retrocession;

- 4.2 have a sound retrocession program that should be guided by the objectives to maximize retention within the country, develop adequate capacity, secure the best possible protection for the retrocession costs incurred and simplify the administration of business;
- 4.3 formulate and execute its overall strategic direction of operations including its retrocession program and review them at least once in a year or whenever there have been material changes in the circumstances under which the retrocession contract was concluded;
- 4.4 put in place appropriate written policies and procedures for its operations, underwriting, accounting, investment and reporting;
- 4.5 put in place tracking, reviewing, monitoring and controlling mechanisms for its entire operations, as part of the overall internal control, risk management and governance structure, that shall be adequate to ensure that:
 - 4.5.1 operations, risk management, internal controls and reporting at a minimum conforms to respective provisions of this Directive,
 - 4.5.2 all underwriting is carried out in accordance with clearly stated policies and procedures,
 - 4.5.3 adequate retrocession cover is in place at all times,
 - 4.5.4 claims are reported to the retrocessionaires and collected timely, followed up and settled in accordance with the retrocession agreement,
 - 4.5.5 for timely settlement of balances due to and from retrocessionaires, and
 - 4.5.6 material deviations from the requirements of this Directive are reported to management and the board as identified;
- 4.6 seek actuarial advices as appropriate to ensure continued soundness of its risk and capital management strategy including at the time it enters into, modifies or terminates a retrocession arrangement;
- 4.7 perform due diligence on retrocessionaires and reinsurance brokers it transacts business with in addition to the requirements stipulated under sub-article 5.2.3 of this Directive;
- 4.8 stipulate and implement procedures and processes to approve, monitor and confirm the



placement of each facultative risk which shall be secured before the commencement date of the policy;

- 4.9 follow procedures for monitoring retention per risk, by line of business and aggregate exposures to ensure that limits or policies or procedures are not breached, including procedures to see that excess concentrations are brought back within the limits or otherwise managed;
- 4.10 promptly inform the National Bank in writing when it became aware of any retrocession issues, including fall in the credit rating of any of retrocessionaires, that could materially impact its financial condition;
- 4.11 ensure that retrocession covers, particularly for large and catastrophic exposures, are adequately addressed and determine whether the retrocession arrangements entered into are sufficient to mitigate losses to acceptable levels as prescribed in the retrocession program;
- 4.12 adhere strictly to the prescription contained in the retrocession treaty for receipts, payments and accounting treatment;
- 4.13 keep separate accounts in respect of long-term reinsurance business and general insurance business and report on each as per the formats prescribed and forming part of this Directive;
- 4.14. submit to the National Bank:
 - 4.14.1. duly completed and separate semi-annual financial returns, non-financial information and schedules of investments in soft copy of plain text and pdf format and hard copy within 30 (thirty) days after the end of half year in the return formats (Annex I, II & III) attached herewith which shall form part hereof, and
 - 4.14.2. annual audited financial statements together with revenue accounts and other supporting schedules within 90 (ninety) days from the close of the financial year; and
- 4.15. prepare annual and semi-annual financial and non-financial returns in the formats prescribed in this Directive.



5. Specific Requirements

5.1. Reinsurance Operations

5.1.1. Statutory Deposit

A reinsurance company shall deposit with the National Bank 15% (fifteen percent) of its paid-up capital in cash or government securities.

5.1.2. Legal Reserve

A reinsurance company shall, at the end of each financial year, transfer to its legal reserve account a sum of not less than 10% (ten percent) of its net profit until such reserve equals its paid-up capital.

5.1.3. Technical Provisions

A) General Reinsurance Business

A reinsurance company at a minimum shall hold technical provisions as follows:

I) Unearned premium provision (UPP) on:

a) gross premium of all:

- i. annual policies and short-term policies shall be calculated using 1/8th method; and
- ii. long-term policies shall be calculated using 1/8th method on the prorated premium.

b) cession:

- i. shall be calculated as per the agreement set out in the retrocession treaty. If the retrocession treaty does not provide such specification, the reinsurance company shall use the method stipulated under sub-article 5.1.3.A.I(a) of this Directive, and
- ii. for all non-proportional treaties (excess of loss and stop loss) shall not be applicable unless special agreement has been concluded with the retrocessionaire.



c) **net premium**

shall be the difference between sub-articles 5.1.3.A.I(a) and 5.1.3.A.I(b) of this article.

II) **Outstanding Claims**

- a) A reinsurance company shall keep and maintain outstanding claims provisions for every insurance and reinsurance arrangement accepted on the basis of loss information advices received from cedants, brokers and where such advices are not received, on an actuarial estimation basis.
- b) Provision for claims under litigation or dispute, at the date of reporting, shall be maintained at 100% of the sum insured or amount disputed or limit of liability, as appropriate, plus the actual or estimated legal costs, and shall be reported together with outstanding claims. However, a separate schedule for such claims shall be maintained by the reinsurance company for reference and follow-up.

III) **Provisions for Incurred But Not Reported (IBNR) Claims**

Provision for incurred but not reported (IBNR) claims shall be 10% (ten percent) of net earned premium or the amount determined by an actuary or the method proposed in writing by an actuary whichever is the higher.

IV) **Other Technical Provisions on:**

a) **Premium:**

- i. other than that determined in accordance with sub-articles 5.1.3.A.I (a), (b) and (c) may be set aside by



supporting it through adequate justification and explanation;

- ii. shall not be mixed up with unearned premium provision (UPP) and be reported separately and independently as required in the return formats; and
- iii. shall be compiled in a separate schedule and delivered to the National Bank upon request.

b) Claims:

- i. shall not be mixed up with outstanding claims and be reported separately and independently as specified in the return formats;
- ii. other than that determined in accordance with sub-articles 5.1.3.A.II (a) and (b) of this Directive may be set aside against adequate and justifiable explanation; and
- iii. shall be compiled in a separate schedule and delivered to the National Bank upon request.

B) Long-term Reinsurance Business

I) Unearned Premium Provision (UPP)

Unearned premium provision for long-term reinsurance business on gross premium, net premium and cession accounts shall either be determined by the method defined by the actuary of the reinsurance company for the purpose of quarterly returns or shall be done by the actuary himself for audited accounts purpose.

II) Outstanding Claims

Outstanding claims on long-term reinsurance business shall be determined as stipulated under sub-article 5.1.3.A.II of this Directive.

Handwritten signature



III) Provision for Incurred But Not Reported Claims

Provision for incurred but not reported (IBNR) claims for long-term reinsurance business shall be determined in accordance with the method specified under sub-article 5.1.3.A.III of this Directive.

IV) Other Technical Provisions

Other technical provisions for long-term reinsurance business shall be determined as stipulated under sub-article 5.1.3.A.IV of this Directive.

5.1.4. Margin of Solvency

A reinsurance company shall keep admitted capital that shall not be less than 20% of net written premium of the preceding 12 (twelve) months.

5.1.5. Liquidity

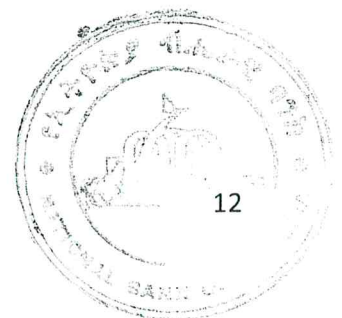
The ratio between admitted current assets and admitted current liabilities shall not fall below 100%.

5.1.6. Investment of Reinsurance Funds

Reinsurance funds shall be invested in the manner prescribed hereunder:

- a. Not less than 60% (sixty percent) of total assets in Treasury Bills and bank deposits provided, however, that aggregate deposits (checking, savings and time deposits) held with any one bank shall not exceed 15% of total assets;
- b. not more than 10% (ten percent) of total assets in purchase or construction of buildings exclusively or predominantly used for rent, capital appreciation; and
- c. not exceeding 20% (twenty percent) of total assets in company shares.

for



5.2 Retrocession Operations

5.2.1 Retention and Cession Limits

A reinsurance company shall set and maintain prudent limit on:

- a) the net amount to be retained per risk, by line of business and aggregate for the whole company. However,
 - i. if the treaty retrocession agreement allows or for clear and justifiable reason(s) the exposure retention exceeds the limit set in accordance with sub-article 5.2.1.(a) of this Directive, it shall be subject to approval by the Board; and
 - ii. the limits must, at least, be based on an evaluation of the reinsurance company's risk profile and the cost of reinsurance;
- b) cessions reflecting security and size of the reinsurance company, and
- c) the maximum foreseeable amount of reinsurance protection to be obtained from approved reinsurance companies.

5.2.2 Aggregate Net Exposure Protection

A reinsurance company shall protect its aggregate net exposure through appropriate reinsurance.

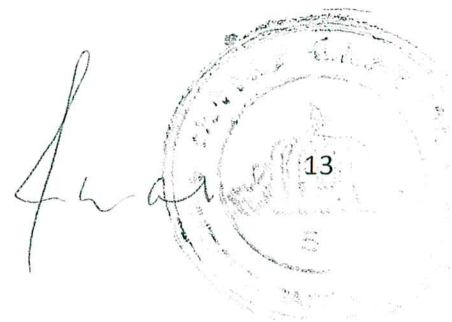
5.2.3 Use of Credit Rating

A reinsurance company shall transact retrocession business with lead and follower reinsurance companies having minimum credit rating of at least "A-" and "BB" or equivalent respectively.

5.2.4 Evidences for Interim Retrocession Arrangement

Until such time of obtaining retrocession contracts, a reinsurance company shall secure duly signed and sealed cover note(s) and/or confirmed slip(s), by respective retrocessionaires, which at a minimum sets out:

- i. the risk(s) retroceded;
- ii. the duration of the coverage;
- iii. the percentage of risk assumed by each retrocessionaire;



- iv. the premium or consideration to be paid by the reinsurance company;
- v. where applicable, any exclusions to terms of coverage; and
- vi. any standard clauses that are to be relied upon or incorporated by reference into the retrocession contract.

5.2.5 Retrocession Contracts

A reinsurance company shall conclude final retrocession contracts, including any amendments thereto within 45 (forty five) days of the effective date of the retrocession coverage. The contract shall bear the signature of the duly authorized persons and the seal of both the reinsurance company and the retrocessionaire(s).

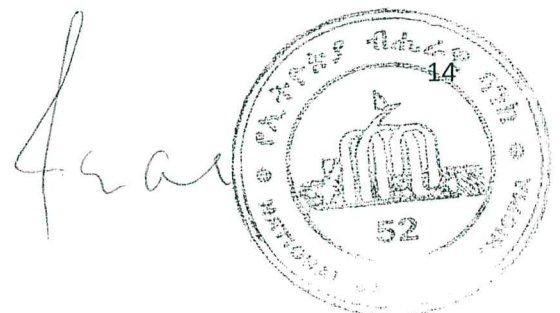
6. Accounting Treatment

- 6.1. Balances due to retrocessionaire(s) shall be paid or cleared in accordance with the terms and conditions of the retrocession agreements.
- 6.2. Claims shall be reported to the retrocessionaire(s) in accordance with the terms and conditions of the retrocession agreements.
- 6.3. Balances due from retrocessionaire(s) shall be collected or settled in accordance with the terms and conditions of the retrocession agreements.
- 6.4. Balances due to and due from retrocessionaire(s) shall be reported separately in the balance sheet.
- 6.5. All retrocession transactions shall be reconciled at least once in a financial year and balances due to and due from, with respect to subsidiary and controlling accounts, shall be clearly documented and reported separately in the interim and audited statements.

7. Documentation on Retrocession

A reinsurance company shall:

- 7.1. maintain at all times a sound and up to date and comprehensive retrocession program, policy and procedures;
- 7.2. document the steps taken to address the adequacy and effectiveness of the retrocession arrangements, particularly for large and catastrophic exposures;



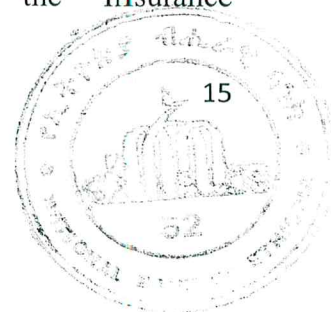
- 7.3. document the manner in which it determines the exposure retention per risk, by line of business and aggregate for the company, including the assumptions underlying the determination;
- 7.4. keep summary of the calculation of expected maximum loss(EML), whenever applied;
- 7.5. maintain documents evidencing the interim retrocession arrangements, such as slip and/or cover note, and retrocession contracts for all classes of business in a timely and orderly manner;
- 7.6. file with the National Bank any new treaty retrocession arrangement, giving full details, documentation, reasons for such an arrangement together with the approval of the board of directors within 15 (fifteen) days of holding the board's meeting. The reinsurance company shall further ensure that the renewal of such a retrocession arrangement coincides with its financial year; and
- 7.7. maintain complete accounting records, statements and schedules for all reinsurance transactions, direct or inward, at a minimum as specified in the format prescribed.

8. Submission of Documents to the National Bank

A reinsurance company shall submit to the National Bank:

- 8.1. soft and hard copies of strategic documents, policies and procedures;
- 8.2. retrocession program within 30 (thirty) days before the commencement of the financial year;
- 8.3. changes made to the strategic document, policies and retrocession program, but in full text, within 15 (fifteen) days after approval by the board;
- 8.4. its retrocession contract, within 60 (sixty) days of the commencement of the financial year;
- 8.5. treaty cover note and/or slip and information on credit rating of lead and follower retrocessionaires together with their share in the reinsurance arrangement, 15 (fifteen) days before the commencement of the financial year; and
- 8.6. further documents, information or explanations with respect to issues that may be raised in connection with all the provisions under this Directive and Insurance Business Proclamation No. 746/2012 as amended by the Insurance

for an



9. Prohibitions

- 9.1. A reinsurance company shall not accept exposures in excess of its limits of retention unless the necessary retrocession arrangements are in place.
- 9.2. Fronting shall be prohibited.

10. Applicability of Laws

All relevant provisions as per sub-article 55(3) of Insurance Business Proclamation No.746/2012 as amended by the Insurance Business (Amendment) Proclamation No.1163/2019 and Directives issued for insurance business shall be applicable.

11. Effective Date

This Directive shall enter into force as of the 1st day of March 2022.

