



STATEMENT OF GUIDANCE

Investment Activities of Insurers

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Statement of Guidance on the Investment Activities of Insurers

1. Introduction

1.1. This document establishes the Cayman Islands Monetary Authority's (the "Authority" or "CIMA") Statement of Guidance on the Investment Activities of Insurers ("Statement of Guidance"). The Statement of Guidance should be read in conjunction with the following:

- a) Rule on Investment Activities of Insurers
- b) Insurance Act, (as amended) and the relevant requirements therein;
- c) Statement of Guidance: Outsourcing Regulated Entities (where applicable);
- d) all relevant insurance regulations; and
- e) any other relevant laws and regulatory instruments issued by the Authority from time to time.

2. Statement of Objectives

2.1. To expand on the regulatory investment requirements issued by the Authority for Insurers, for the purpose of ensuring Insurers make appropriate investments that consider all relevant risks. This Statement of Guidance will:

- a) set out the expectations of the Authority regarding compliance with the Rule on Investment Activities of Insurers; and
- b) highlight key considerations that should be taken into account by Insurers in devising an investment strategy, including ensuring that assets are managed in a sound and prudent manner consistent with the risk profile of the Insurer and its liquidity needs.

3. Statutory Authority

3.1. The measure is consistent with the Authority's statutory objectives as prescribed in the Monetary Authority Act (2020 Revision) (as amended) ("MAA") at Section 34(1)(a) which states that:

*"After private sector consultation and consultation with the Minister charged with responsibility for Financial Services, the Authority may –
(a) issue or amend rules or statements of principle or guidance concerning the conduct of licensees and their officers and employees, and any other persons to whom and to the extent that the regulatory laws may apply."*

4. Scope of Application

4.1. This Statement of Guidance applies to all Insurers and registered Portfolio Insurance Companies supervised by the Authority in accordance with the Insurance Act (as amended).

5. Definitions

- 5.1. The following definitions are provided for the purpose of this Statement of Guidance:
- 5.1.1. **“Capital and Solvency Regulations”** means The Insurance (Capital and Solvency) (Class A Insurers) Regulations, 2012 and the Insurance (Capital and Solvency) (Classes B, C and D Insurers) Regulations (2018 Revision).
 - 5.1.2. **“Insurer”** has the meaning assigned in section 2 of the Insurance Act and includes Portfolio Insurance Companies registered under the Insurance Act (as amended).
 - 5.1.3. **“Investment Committee”** means a committee established by the Insurer for the purpose of maintaining the Insurer’s Investment Policy and overseeing its investment activities consistent with the Rules and Statement of Guidance on Investments Activities of Insurers.
 - 5.1.4. **“Investment Policy”** means documented criteria, processes, and procedures for implementing an Insurer’s investment strategy.
 - 5.1.5. **“Investment Strategy”** means the methods to be used by an Insurer in meeting its overall investment objectives.
 - 5.1.6. **“Related Business”** has the meaning assigned in section 2 of the Insurance Act.
 - 5.1.7. **“Regulatory Laws”** refer to Acts delineated in section 2 of the Monetary Authority Act (as amended).

6. Guidance on General Principles

Security

- 6.1. Investments should be sufficiently secure for the portfolio as a whole, which is essential in ensuring obligations to policyholders can be met. To assess the security of its investments, an Insurer must ensure that it has assessed the nature, scale and complexity of the associated risks.
- 6.2. The security of an investment is related to the protection of its value and can be affected by credit and market risks. It may also be affected by safekeeping, custodianship, or trusteeship. Assets must be held in an appropriate location, so they are available to meet policyholder claims where policyholder payments are made. Assets held out of the Cayman Islands must be under the secure control through direct means or through the terms and conditions of trust deeds, treaties or other contractual agreements by an Insurer and/or its appointed insurance manager, where applicable.
- 6.3. Further, where assets are held and/or managed by related parties on behalf of an Insurer, the Insurer should put in place the appropriate controls to manage all conflicts of interest.

Liquidity

- 6.4. An Insurer should ensure that its assets generate sufficient cash flows to pay policyholder claims when due as well as all other obligations.
- 6.5. An Insurer's ability to maintain liquidity must include considerations such as:
 - 6.5.1. unexpected large claims;
 - 6.5.2. an event resulting in many claims;
 - 6.5.3. significant shifts in investment market conditions; and
 - 6.5.4. obligations relating to derivatives positions and what arrangements will be put in place to mitigate such occurrences.

Diversification

- 6.6. Investing in a wide range of assets enables the Insurer to mitigate the risk of adverse financial events.
- 6.7. It is important that the Insurer's overall investment portfolio is adequately diversified (where applicable) and that its assets and counterparty exposures are kept to prudent levels. The Authority expects that the diversification of assets in an Insurer's portfolio will fit the risk profile having regard to the type of business undertaken by the Insurer and the relevant prescribed capital requirements in the Capital and Solvency Regulations.
- 6.8. An Insurer's investment portfolio should be diversified within and between risk categories considering the nature of the liabilities.
- 6.9. An adequate mix of investment categories should contemplate:
 - 6.9.1. the risk profile/default risks/impairment of investments;
 - 6.9.2. the investment horizon (i.e. duration of the investment);
 - 6.9.3. the correlation of the asset classes;
 - 6.9.4. liquidity of assets; and
 - 6.9.5. the Authority's statutory solvency requirements.
- 6.10. Unless otherwise required by the Regulatory Laws , to generally ensure that its investment portfolio is adequately diversified, an Insurer should avoid overreliance on any specific asset type, issuer, counterparty, group or market and any excessive concentration or accumulation of risk in the portfolio.

Risk Management

- 6.11. An Insurer should consider various internal and external factors that are likely to affect the investment risks it is exposed to, including, its risk tolerance levels, its objectives, the general economic climate, interest rates, legal and regulatory requirements.
- 6.12. An Insurer should evaluate and understand the source, scope and types of risks associated with an investment activity and implement adequate procedures to manage investment risks, while giving consideration to the interrelationships and interdependencies between the risks to which the Insurer may be exposed. Consideration should be given to implementing adequate methods/tools to be used to measure the risk exposure and establish techniques¹ for mitigating those risks.

¹ "Techniques" for example, may include assessing the investment manager of an investment fund.

7. Asset Liability Management

- 7.1. Asset Liability Management allows decisions and actions taken with respect to assets and liabilities to be coordinated through the ongoing process of formulating, implementing, monitoring and revising strategies related to assets and liabilities in order to achieve an Insurer's financial objectives, given its risk tolerance and other constraints, such as duration, volatility and real growth prospects to counter currency instability and claims inflation.
- 7.2. An Insurer's investment policy should therefore address:
 - 7.2.1. how the investment and liability strategies adopted by the Insurer allow for interaction between assets and liabilities, including liability mitigation strategies;
 - 7.2.2. a consideration of the correlation of risk between different asset classes as well as the correlation between different products and business lines;
 - 7.2.3. how the liability cash outflows are met by the cash inflows; and
 - 7.2.4. how the economic valuation of assets and liabilities are changed under a range of different scenarios including the implications of the accounting regime in place.

8. Investment Committee

- 8.1. The Investment Committee shall be composed of at least one member of the Board with expertise on investment/financial matters in addition to other competent representatives appointed by the Board who may include related persons holding senior management roles, or equivalent third parties.
- 8.2. The requirement for the establishment of an Investment Committee does not apply to Class B(i) and B(ii) Insurers.
- 8.3. The duties of the Investment Committee, as approved by the Board, are to include at a minimum the implementation and oversight of adequate risk management systems and controls in respect of the investments of the Insurer including ensuring that:
 - 8.3.1. there is a proper segregation of execution, monitoring and performance measurement functions;
 - 8.3.2. persons entering, performing or otherwise dealing in investments for and on behalf of the Insurer, and any limits on such authority are clearly delineated;
 - 8.3.3. there are proper performance monitoring procedures in place, which facilitate the regular conduct of measurement and valuation of investment performance;
 - 8.3.4. there are continuous risk monitoring procedures, commensurate with the nature, size, and complexity of the Insurer's investment activities;
 - 8.3.5. there is timely management reporting;
 - 8.3.6. the investments of the Insurer are handled by qualified and properly trained persons capable of assessing the nature, scale and complexity of the associated risks of investment activities of the Insurer;
 - 8.3.7. there are sound internal audit procedures to ensure compliance with the Insurer's policies and procedures and statutory requirements, the internal audit procedures may be conducted through independent and competent internal arrangements such as internal audit and/or

compliance functions, or through equivalent independent and competent third parties; and

- 8.3.8. that the use of complex investments (based on a review of various scenario analyses), does not jeopardize the value preservation of the total assets or the tied assets or the Insurer's solvency.

9. Investment Policy

- 9.1. An Insurer's investment policy should be commensurate with the nature, size and complexity of its insurance business activities. The policy should, where possible, identify the due diligence processes that will be utilised for each investment, identify the manner by which appropriate credit ratings for each investment (together with an independent credit analysis) will be conducted including details of the investment process from start to finish.

10. Internal Controls

- 10.1. Insurers should establish adequate systems of internal control to ensure that assets are managed in accordance with the overall investment policy.
- 10.2. Internal controls for investment activities could include:
- 10.2.1. concentration limits;
 - 10.2.2. valuation and recording of investments in accordance with generally accepted accounting principles;
 - 10.2.3. cash flows generated through investments such as income, repurchases and redemptions at maturity; and
 - 10.2.4. reporting on investments.
- 10.3. The Insurer should ensure that its internal controls are consistent with established policies and procedures as well as the adequacy of the internal and external audit functions relative to its size and risk profile.
- 10.4. Where an Insurer has outsourced its investment management function, consideration should be given to the Authority's Statement of Guidance on Outsourcing.

11. Use and Reliance on External Credit Ratings

- 11.1 In the absence of credit ratings from recognised rating agencies, an Insurer should conduct independent credit analysis to ensure adequate assessment in respect of the security of the investment.

12. Credit Review for Loans

- 12.1 Insurers that propose to engage in investment activity involving the provision of a loan (or equivalent extension of credit) are required to seek prior approval from the Authority for each loan (or equivalent extension of credit). The procedure for such approval request is outlined in *Regulatory Procedure – Approval and Notification of Changes – Class B, C and D Insurers and Portfolio Insurance Companies*.

- 12.2 In submitting a request to the Authority to grant a loan (or the equivalent extension of a credit), an Insurer must submit material details regarding the loan, including, the purpose, terms and conditions of the loan. Depending on the nature of the loan and the parties involved, the Authority may require a draft loan agreement to be provided. The request should provide an explanation of the risk assessment conducted by the Insurer on the borrower and details as to whether collateral is required to support the loan.
- 12.3 The provision of loans should not be a significant part of an Insurer's business operations. The Authority will review a request for provision of loans on a case-by-case basis and may prohibit or restrict the amount of loans held by an Insurer.
- 12.4 The scope of the Rule and Statement of Guidance relate to investment activity of the Insurer and therefore is not intended to cover loans proposed to be issued by an Insurer for other commercial purposes or to related parties and affiliates. Insurers are not licensed as lending financial institutions and are therefore prohibited from selling loan products unless otherwise approved by the Authority as part of the Insurer's Business Plan.
- 12.5 Loans granted to related parties and affiliates for non-investment purposes e.g. to provide liquidity relief to such parties are also out of scope of the Rule and Statement of Guidance and such loans would also require prior approval from the Authority on a case-by-case basis as a Business Plan change as stipulated in the Insurance Law. The procedure for such approval request is outlined in *Regulatory Procedure – Approval and Notification of Changes – Class B, C and D Insurers and Portfolio Insurance Companies*.

13. Derivatives

- 13.1. Insurers that propose to invest in derivatives for non-hedging or speculative purposes are required to seek prior approval from the Authority. Details of such proposed investments should be included in the insurers investment policy that is submitted to the Authority. When approved by the Authority as part of the investment policy, the Insurer will not be required to seek approval from the Authority when executing individual trades as long as the set maximum limits are not exceeded. To the extent that non-hedging or speculative derivatives investments are incorporated subsequent to the submission of the investment policy, approval by the Authority would be required as a Business Plan change as stipulated in the Insurance Law. The procedure for such approval request is outlined in *Regulatory Procedure – Approval and Notification of Changes – Class B, C and D Insurers and Portfolio Insurance Companies*.
- 13.2. An Insurer should evaluate the security of derivative products by taking into account the underlying exposures, as well as the security of the derivative counterparty, the purpose for which the derivative is held, and the cover (such as collateral) the Insurer has for derivative exposure.
- 13.3. An Insurer should ensure its investment policy provides adequate steps/procedures on the use of derivatives including the purpose for which derivatives will be used and the rationale for undertaking different types of transactions.
- 13.4. The Investment Committee should therefore be charged with the responsibility of:

- 13.4.1. ensuring that derivatives use aligns with the objectives and policies of the Insurer as identified in the Insurer’s investment policy;
- 13.4.2. assigning resources with sufficient expertise to analyse and monitor the risk of all transactions taken by the Insurer individually and in aggregate; and
- 13.4.3. maintaining thorough records for all derivative transactions and that can be made readily available to the Authority, if requested.

14. Effective Date

- 13.5. This Guidance will come into effect within twelve months from the date that it is published in the Gazette.



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