



Republic of the Philippines  
Department of Finance  
**INSURANCE COMMISSION**  
1071 United Nations Avenue  
Manila



Circular Letter (CL) No.:	2018-18
Date:	09 March 2018
Superseding:	CL No. 2016-67
Amending:	CL No. 2015-06

### CIRCULAR LETTER

**TO : ALL NON-LIFE INSURANCE COMPANIES AND PROFESSIONAL REINSURANCE COMPANIES DOING BUSINESS IN THE PHILIPPINES**

**SUBJECT : VALUATION STANDARDS FOR NON-LIFE INSURANCE POLICY RESERVES**

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Pursuant to Sections 219 and 220 of the Amended Insurance Code (Republic Act No. 10607) which require every insurance company other than life to maintain (a) a reserve for unearned premiums on its policies in force, and (b) the estimated amount of all its other liabilities including taxes, expenses and other obligations due or accrued including any special reserves required by the Commissioner, in addition to its liabilities and reserves on contracts of insurance issued by it, attached is the revised Valuation Standards for Non-Life Insurance Policy Reserves which shall take effect retroactively starting 01 January 2017.

This Circular supersedes Circular Letter (CL) No. 2016-67 and amends CL No. 2015-06 "New Reserves Computation for the Compulsory Insurance Coverage for Migrant Workers".

For strict compliance.

  
**DENNIS B. FUNA**  
Insurance Commissioner



# **VALUATION STANDARDS FOR NON-LIFE INSURANCE POLICY RESERVES**

## **1 Introduction**

- 1.1 Every non-life insurance company or reinsurance company supervised by the Insurance Commission (IC) shall maintain reserves for its written policies, which shall be charged as a liability in any determination of its financial condition, as required by the IC, in accordance to Sections 219 and 220 of the New Insurance Code (RA 10607), as well as this Valuation Standards for Non-Life Insurance Policy Reserves.

## **2 Scope and Application**

- 2.1 This Valuation Standards shall apply to all policies issued by non-life insurance companies and reinsurance companies.
- 2.2 This Valuation Standards is intended to cover both direct and assumed reinsurance business, whether treaty or facultative, of non-life insurance companies.

## **3 Key Definitions**

- 3.1 In this Valuation Standards, unless the context otherwise requires:
  - 3.1.1 "Company" refers to a non-life insurance company or reinsurance company supervised by the IC.
  - 3.1.2 "Actuary" refers to an in-house actuary of the Company or an external consulting actuary accredited by the IC.
  - 3.1.3 "Policy Reserves" refers to the aggregate of Premium and Claims Liabilities both defined below.
  - 3.1.4 "Premium Liabilities" refers to all future claim payments and related expenses for policy maintenance and claims settlement, to be made after the valuation date, arising from future events for which the Company is liable under its insurance contracts, and is computed on both gross and net of reinsurance basis.

- 3.1.4.1 "Unearned Premium Reserves" or "UPR", refers to the amount of reserve for that portion of the premium received which is attributable to a period of risk falling beyond the valuation date.
- 3.1.4.2 "Unexpired Risk Reserves" or "URR", refers to the amount of reserve required to cover future claims and expenses, at a designated level of confidence, that are expected to emerge from an unexpired period of cover.
- 3.1.5 "Claims Liabilities" refers to claims incurred but not yet paid as of valuation date, for both the Company's direct and assumed reinsurance business, whether treaty or facultative. It includes claims due and unpaid, claims in the course of settlement, resisted claims and those which are incurred but not reported at a designated level of confidence, as well as direct and indirect expenses related to settling all outstanding claims, whether reported and unreported, as of valuation date.
- 3.1.5.1 "Outstanding Claims Reserve" refers to the estimated amount of reported claims that have not yet been settled as of valuation date.
- 3.1.5.2 "Incurred but not Reported" or "IBNR", refers to the amount to be provided for claims in respect of claim events that have occurred but have not been reported to the company as of the valuation date.
- 3.1.5.3 "Claims Handling Expense" refers to the estimated amount of expenses for settling all claims, whether reported or unreported, outstanding as of valuation date applicable to both direct business and assumed treaty and facultative reinsurance businesses.

## **4 Data and Systems**

- 4.1 The Company's Chief Executive Officer (CEO) or a Responsible Officer with a comparable rank shall ensure that the Company's database is properly maintained so that the premiums and claims data provided to the Actuary is accurate and complete. The CEO or the Responsible Officer must furnish the data to the Actuary and must allow his/her Actuary reasonable access to the Company's database.

- 4.2 The Actuary shall apply reasonable tests to satisfy himself that the premiums and claims data is accurate and complete. A check for both integrity and completeness of data should precede the valuation work. Furthermore, the Company shall maintain a historical claims database of at least ten (10) years.
- 4.3 The Company shall create loss development triangles on both paid and incurred claims for each class of business, on both gross and net of reinsurance basis. The length of historical data needed in creating the loss development triangles must be based on the Company's underlying business and on the long-term development of each class of business. Please refer to **Annex D**.
- 4.4 Companies or specific classes of business which have insufficient data as a result of business expansion or mergers and acquisitions shall be required to use as much data as they currently have until they have accumulated the appropriate length of historical claims data for valuation purposes.
- 4.5 The Company shall maintain a database of historical claims, on both gross and net of reinsurance basis, pertaining to large loss events incurred for as long a period as the loss development triangles, for the purpose of measuring and monitoring catastrophic risks, as described in Section 11 below.
- 4.6 The Company shall also maintain records on historical earned and unearned premiums for each class of business, on both gross and net of reinsurance basis, as well as commissions and other expense information in relation to policy maintenance and claims settlement, for the purpose of estimating future expenses for valuation of policy reserves.
- 4.7 The Company shall determine the claims grouping for valuation of policy reserves on either an accident year or an underwriting year basis per class of business, whichever is more appropriate, and prepare the corresponding data to the determined basis.

## 5 Basis of Assumptions

- 5.1 As much as practicable, the valuation of policy reserves shall be based on the Company's actual historical experience and/or industry data. Any deviations and the use of professional judgment must be supported by a

strong rationale and must be documented in Section C of the Actuarial Valuation Report, as described in **Annex A**.

- 5.2 Premiums used in the valuation of policy reserves shall be gross of expenses, commissions, taxes, etc. depending on the Company's discretion.
- 5.3 Premiums and claims data used in the valuation of policy reserves, as well as projection of future claims, shall be on gross and net of reinsurance basis.
- 5.4 The Actuary shall gather information from the Underwriting Department or its equivalent to provide information on the following areas: market outlook, changes in pricing levels, impact of historical and current catastrophes, level of reinsurance cover, policy inception profile, changes in the mix of business, renewal rates and changes in terms and conditions.
- 5.5 The Actuary shall also gather information from the Claims Department or its equivalent to provide information on the following areas: typical claims process from notification to settlement, current key uncertainties with reaching settlement of claims, claims expense inflation, large loss experience, operational changes in the claims function, large loss concerns and uncertainties, and changes in initial case estimates.
- 5.6 The Company's projection of future claims shall be based on the loss development triangles per class of business, as described in paragraph 4.3, as well as the results of the information gathered from Underwriting and Claims Departments, or their equivalents, as described in paragraphs 5.4 and 5.5.
- 5.7 The Company shall determine the major classes of business in its operations for reserving purposes by performing a risk assessment process. At a minimum, the Company shall define its classes of business as follows: Fire, Marine, Casualty, Motor Car and Suretyship. However, the Company can come up with a more granular classification based on its own risk assessment.

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## 6 Valuation Methodology

- 6.1 The Actuary, as set out in the New Insurance Code, shall be responsible to determine the level of policy reserves using basis no less stringent than that prescribed in Sections 7 to 10 below.
- 6.2 The reserves for a non-life insurance company shall be composed of Premium and Claims Liabilities both determined using best estimate assumptions, with an appropriate Margin for Adverse Deviation (MfAD) for expected future experience.

## 7 Premium Liabilities

- 7.1 Premium Liabilities shall be determined on an aggregate basis.

A computation should be performed to determine whether the URR required is greater or smaller than the UPR net of Deferred Acquisition Cost (DAC). If the URR is greater, then the difference should be booked as an additional reserve on top of UPR.

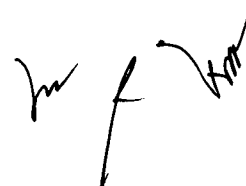
Therefore, Premium Liabilities is equal to the UPR plus the difference between the URR and the UPR net of DAC, if the URR is greater than the UPR net of DAC. Otherwise, it is equal to the UPR.

- 7.2 UPR shall be calculated based on the 24<sup>th</sup> method for all classes of business, on both gross and net of reinsurance basis. This means that for policies with policy duration of less than one (1) year or more than one (1) year, the UPR shall consider the actual unearned premium from the date of valuation to the date of termination of the policy. Further, the same method in the calculation of the UPR shall apply to policies covering migrant workers/Overseas Filipino Workers (OFWs) using the Table of Premiums for Reserve Computation stipulated in Annex A of CL No. 2015-06 until the said CL is further amended. The Actuary shall provide sufficient basis for any material deviations from this methodology in Section C of the Actuarial Valuation Report, as outlined in **Annex A**.
- 7.3 URR shall be calculated as the best estimate of future claims and expenses for all classes of business, with MfAD as computed in Section 9. This best estimate relates to expected future claim payments and related expenses to be incurred after the valuation date, arising from future events.

- 7.3.1 Expected future claims shall include all claims which might occur during the unexpired period including: claims which are reported after the end of the unexpired exposure period, but have occurred within the unexpired exposure period; and claims which are reopened at any date, but have occurred within the unexpired exposure period.
- 7.3.2 Expected future expenses shall include policy maintenance expenses and claims management expenses (i.e., direct and indirect claims settlement costs).
- 7.4 The URR may be estimated as the unearned premium for each class of business multiplied by the ultimate loss ratio, adjusted for future expenses and MfAD.
- 7.5 The Actuary may consider an adjustment of the ultimate loss ratio by allowing for large and catastrophic losses; however, these should be captured on a best estimate basis considering the severity apportioned by the expected frequency of such a loss.

## **8 Claims Liabilities**

- 8.1 Claims Liabilities for both direct business and assumed treaty and reinsurance businesses shall be calculated as the sum of Outstanding Claims Reserve, Claims Handling Expense and IBNR, with MfAD as computed in Section 9.
- 8.2 Outstanding Claims Reserve shall be based on actual claims reported but have not yet been settled as of valuation date. The Company shall ensure integrity of the data inputs as well as minimize uncertainties in the claims processing, subject to paragraph 4.2.
- 8.3 The IBNR shall be calculated based on standard actuarial projection techniques or combination of such techniques, such as but not limited to the chain ladder method, the expected loss ratio approach, and the Bornhuetter-Ferguson method. The Actuary shall determine the appropriateness of the methodology considering the characteristics of the data, such as maturity of the business.

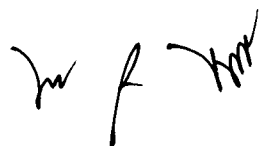
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- 8.4 Claims Liabilities shall also include a provision for Claims Handling Expenses, which covers the estimated expenses of settling all claims, both reported and unreported, outstanding as of valuation date.
- 8.5 The Actuary shall ensure the reliability of the expected loss ratios by obtaining estimates from various sources, such as underwriters, the business plan, pricing actuaries, market statistics, or from a historic view of profitability and loss ratios.
- 8.6 In valuing the Claims Liabilities, the Actuary should consider other factors such as but not limited to: varying expense structure in run-off situations, large losses arising from significant past events, operational changes in claims management, underwriting changes such as business mix and premium rate changes, changes in reinsurance program, changes in claims handling process, and external conditions.
- 8.7 To ensure sufficiency of reserves, the Actuary shall conduct a back-testing exercise of the IBNR by comparing the previous year's IBNR of expected current year claim developments, with actual current year claim developments. The results of such shall be documented in Section D of the Actuarial Valuation Report, as outlined in **Annex A**. In cases where the IBNR has proven insufficient to cover actual claims development, the Actuary shall revisit the assumptions for IBNR valuation and document the rationale for this deterioration.

## 9 Margin for Adverse Deviation

- 9.1 The Company shall include an MfAD to allow for inherent uncertainty of the best estimate of the policy reserves. The purpose of the MfAD is to consider the variability of claims experience within a class of business, the diversification between classes of business and conservatism in the best estimate.

The actuary shall determine the company-specific MfAD on at least an annual basis based on standard projection techniques or combination of such techniques, such as but not limited to the Mack Method, Bootstrapping Method, Stochastic Chain Ladder Method to bring the actuarial estimate of the Policy Liabilities at the 75<sup>th</sup> percentile level of sufficiency. The data, basis and analysis in the determination of the MfAD shall be included in Annex A





## 10 Discounting

10.1 The Actuary shall determine the materiality of discounting the cash flows in calculating the policy reserves. It shall be emphasized that cash flow timing is based on claims delay pattern and not on policy maturity.

10.2 If the Actuary deems it material to discount the cash flows in computing the policy reserves, the Actuary shall use current risk-free rates. The rates shall exactly match the duration of the policy and the currency of the cash flows and shall be prescribed by the IC.

## 11 Monitoring of Severe and Catastrophic Risks

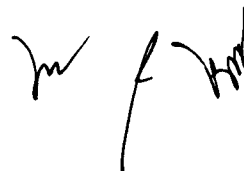
11.1 Companies shall take measures to ensure proper monitoring of risks beyond the 75<sup>th</sup> percentile confidence level, such as internal modelling or performance of appropriate stress testing exercises.

## 12 Actuarial Valuation Report

12.1 The Actuary shall prepare an actuarial valuation report to be submitted to the IC. The actuarial valuation report, at a minimum, shall contain the following information (see **Annex A** for details):

- (i) Scope of Report
- (ii) Data Requirements
- (iii) Valuation Methodologies and Assumptions
- (iv) Analysis of Experience
- (v) Valuation Results
- (vi) Certification by the Actuary
- (vii) Certification by the CEO or Responsible Officer

12.2 The Certifications to be provided by the Actuary and the CEO or Responsible Officer shall be duly notarized.



**Report on Actuarial Valuation of Non-Life Insurance Policy Reserves**

**Name of Company:** \_\_\_\_\_

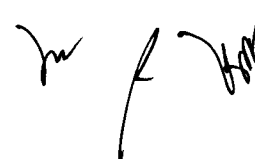
**For the period ended dd/mm/yyyy**

**Section A: Scope of Review**

1. Purpose of report
2. Name of Actuary (whether the Actuary is an employee of the insurance company or an external consultant), professional qualifications, and the capacity in which he/she is carrying out the valuation of policy reserves
3. Confirmation from the Actuary of compliance with requirements with this Valuation Standards, and reasons, if any, for not complying fully with any requirements

**Section B: Data Requirements**

1. The basis on which the analysis has been carried out (i.e., underwriting or accident year)
2. The source of the data and how it was extracted
  - a. Description of the company's current underwriting policies: specific market segments targeted, risk selection process, any major recent changes in premium rates and policy conditions, any recent changes in levels of underwriting authorities, any recent changes in key personnel and delegation of authority, and any changes in level of deductibles or policy limits
  - b. Description of the company's claims management policies: guidelines for case reserving and the use of loss adjusters, policies on opening and closing of claims, operational changes in claims function, large loss concerns and uncertainties
3. Documentation of any adjustments made to the data to allow for abnormal items such as large losses, catastrophe losses, etc. including the nature, amount and rationale for the adjustment
  - a. Description of significant events during the year affecting the claim experience and how these were taken into account in the valuation of the liabilities
  - b. Description of other effects considered including economic, technological, medical, legislative environment, social trends, competition, court decisions, consumerism, etc.



4. Documentation of quantitative information which may have an impact on valuation, if applicable

### **Section C: Valuation Methodologies and Assumptions**

1. Detailed discussion on the valuation methods, assumptions, and professional judgment used in the estimation of the following:
  - a. Premium liabilities
  - b. Claims liabilities
  - c. Claims handling expense and other related expenses
  - d. Margin for adverse deviation
  - e. Discounting, if applicable
2. When more than one method is used, the basis for choice of results
3. Justification for key differences in assumptions between valuations of premium and claims liabilities
4. Any material deviations from this Valuation Standards in terms of valuation methodologies and assumptions, and basis for these deviations

### **Section D: Analysis of Experience**

1. For year-end valuation, detailed analysis of the company's actual experience of both URR and claim liabilities versus expected experience in previous year-end valuations, including justifications for any material change observed. The experience analysis should cover claims payments and incurred cost movement.
2. Comparative analysis between current and previous valuations such as discussion of reserve movements.

### **Section E: Valuation Results and Discussion**

The summary of the valuation results shall follow the format shown in **Annexes B.1, B.2 and C**. Companies shall provide a short narrative discussing their valuation results for each class of business.



## **Section F: Certification by the Actuary**

The Actuary shall provide a duly-notarized certification as set out below:

"I hereby certify that I have conducted tests necessary to verify the reasonableness and integrity of the data, confirm that the information contained in this Report are accurate to the best of my knowledge and that I have calculated the policy reserves in accordance with the Valuation Standards prescribed by the Insurance Commission and the standards of practice of the Actuarial Society of the Philippines."

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Signature over Printed Name of Actuary

Date: \_\_\_\_\_

IC Accreditation No.: \_\_\_\_\_

PTR No.: \_\_\_\_\_

## **Section G: Certification by the CEO or Responsible Officer**

The CEO/Responsible Officer shall provide the following duly-notarized certification:

"I hereby certify that the database is properly maintained and I have satisfied myself that the data provided to the certifying Actuary are accurate and complete."

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Signature over Printed Name of  
Chief Executive Officer/Responsible Officer

Date: \_\_\_\_\_

