



Asian Development Bank

# Memorandum

Southeast Asia Department  
Public Management, Financial  
Sector, and Trade Division

10 December 2013

## For Approval of Para. 14

To: James Nugent *[Signature]* 13 Dec '13  
Director General, SERD

Through: *[Signature]* Shigeko Hattori  
Director, SEPF

From: *[Signature]* Madeleine Varkay  
Principal Private Sector Development Specialist, SEPF

Subject: **P47207-001 PHI: Capacity Development to Support Regulation and Oversight at the Insurance Commission**  
**— Approval of Small-scale Technical Assistance Project**

## I. INTRODUCTION

1. The proposed Small-scale Technical Assistance (SSTA) builds on a series of policy recommendations developed under ADB Program Loans<sup>1</sup> to address the institutional shortcomings of the Philippines Insurance Commission.<sup>2</sup> The SSTA will support the Insurance Commission's (IC) expanded functions through specific staff training and Information Technology (IT). The SSTA will thereby strengthen the supervisory functions of the Insurance Commission in preparation for the Earthquake Insurance project scheduled for Board approval in 2014.

2. At present, the Philippine insurance market remains small<sup>3</sup> but consists of a large number of companies. The low capital requirement is being amended under the new Insurance Code which should foster industry consolidation in anticipation also of the ASEAN Free Trade Agreement in Services. Insurance penetration is low with an estimated 23 % of the population (22 million people out of 97.60 million) having insurance policies. Despite the large number of

<sup>1</sup> In 2006, Program Cluster, Loan, including Technical Assistance Grant Financial Market Regulation and Intermediation Program (Philippines), undertook capacity building on risk-based supervision. In 2010, Subprogram 2 - Financial Market Regulation and Intermediation Program Loan (Philippines), defined (i) the need for the IC to strengthen its risk-based formula in line with international standards, (ii) the restructuring of the IC by the Department of Finance to (a) adjust salary scales in line with relevant positions in the financial sector; and (b) increase resources to support the agency's oversight function.

<sup>2</sup> The TA first appeared in the ADB Business Opportunities website on 10 December 2013.

<sup>3</sup> The total assets of the insurance industry are Php780.17 billion assets or 7.60% of the banks' total assets of Php10.23 trillion. The life insurance sector dominates the sector with 34 companies accounting for 79.56% of overall industry assets, followed by the property and casualty sector where 81 companies account for 16.26% of the market, and the Mutual Benefit Associations (MBAs) where 26 MBAs account for 4.18% market share. Total Industry Premium Volume – P150.38 billion of which, Life Sector = Php120.30 billion (80% share); Non-Life Sector = P26.94 billion (18%); MBA Sector = P3.14 billion (2% share).

companies, premium volume was 1.42% of GDP in 2012. The Philippines ranks 5<sup>th</sup> in the region in terms of insurance penetration, after Singapore, Malaysia, Thailand and Indonesia. The sector was liberalized in 1994 allowing foreign firms to own 100% equity stakes in insurers and to enter the market by either a local joint venture or setting up a local subsidiary or branch. The five<sup>4</sup> largest life insurance companies dominate the market (70% of premiums written in 2012). In the nonlife insurance sector, where a large number of companies are small, family owned entities, the ten largest companies account for 55% of net premiums written in 2012. The country has one domestic reinsurance company. Two companies are rated internationally by AM Best, these are: Malayan Insurance Co. Inc. upgraded to "bbb+" Insurance's issuer credit rating (ICR) and "B++" (good) financial strength rating (FSR) and National Reinsurance Corporation of the Philippines, rated "bbb" and "B++" respectively, as of May 2013.

3. The supervision of the pre-need industry was transferred in 2010 from the Securities and Exchange Commission (SEC), where the institutions were regulated as deposit taking or brokerage entities, to the Insurance Commission where they are presently regulated as institutions with actuarial liabilities paying contingent benefits. Many of the companies are insolvent; of the 51 that were transferred to the Insurance Commission, a large number have been placed under liquidation (30), while the licenses of those remaining are being reviewed under an ongoing ADB TA<sup>5</sup>. The pre-need sector provides funeral and burial services, as well as education, pension and life insurance policies. While some products are for fixed amounts, others (in the funeral services and education fields) are open-ended.

4. Moving forward, the major challenges for the Insurance Commission will be to preside over industry consolidation in the non-life sector, as well as liquidation in the pre-needs sector. At present, the Insurance Commission is systematically examining company paper-based audited financial reports, however, due to the lack of an integrated Information Technology (IT) system, there is a backlog in the examiners' analysis of the statements.

5. Until recently, the insurance sector in the Philippines has been governed by the outdated Insurance Code (1974), which has restricted the Insurance Commission's<sup>6</sup> ability to enforce the law and regulations, due to weak legal protection of supervisors and staff, hampered its ability to hire professionally qualified staff as a result of the salary standardization law, and thereby constrained the reorganization and upgrading of its management structure and supporting business processes. During the current administration, the newly designated Insurance Commissioner, a professional actuary and former life insurance executive, has initiated the amendment to the Insurance Code and taken several major steps to achieve effective supervision by reorganizing the Insurance Commission from a functional setup with no information flow between units, to an organizational structure led by four deputy commissioners, with defined responsibility in the area of technical services, financial examination, management support services as well as legal and regulatory supervision.

<sup>4</sup> These include, Pru Life Insurance Company of the UK, BPI Philam Life Assurance, Sun Life of Canada, and Philippine AXA Life as well as Philippine American Life and General Insurance.

<sup>5</sup> PHI: Capacity Development of Financial Regulators - TA 8038, is providing assistance to the Insurance Commission on improving the potential viability of the 14 companies that are still active, developing proposals for liquidation or resolution, as well as plans for an equitable treatment on behalf of plan holders in failed institutions. The TA is also outlining the organization and functions of the pre-needs division.

<sup>6</sup> The Insurance Commission, a government agency under the Department of Finance, supervises and regulates the operations of life and nonlife companies, mutual benefit associations, and trusts for charitable uses. It issues licenses to insurance agents, general agents, resident agents, underwriters, brokers, adjusters, and actuaries; and has the authority to suspend or revoke such licenses. The commission currently has 216 staff.

6. As of February 2013, the Philippine Senate and House of Representatives passed the consolidated Bill amending the Insurance Code and submitted for its approval by the President. The amendments and additional provisions in the Insurance Code, include the following: (i) minimum capital / solvency requirements for insurance companies increased from P250 million by end-2012 to P1.2 billion by year-end 2022; (ii) the Insurance Commissioner, now appointed by Presidential Order, for a fixed term of six years, has authority over disputes of up to P5 million; (iii) license issued to insurance companies is extended to three years<sup>7</sup>; (iv) expanded the range of investment instruments / assets admitted in the computation of equity<sup>8</sup>; (v) new provisions on microinsurance, bancassurance (together with Bangko Sentral ng Pilipinas), and financial reporting framework. The Insurance Commission is preparing rules and regulations concerning the following: (i) new solvency requirement for life and non-life companies; (ii) premium deposit fund (deposit of payments); (iii) self-regulatory organization; (iv) trust business of insurance companies; (v) alternative dispute resolution (ADR) methods; (vi) increased fees, charges and fines; (vii) electronic policy forms and processes.

## II. ISSUES

7. To assist with the timely implementation of the Insurance Code, and strengthen the supervisory functions of the regulator, the Insurance Commissioner has identified the following areas for capacity building: (i) knowledge and skills training on the risk-based capital<sup>9</sup> requirements; (ii) upgrading of the Insurance Commission's IT to support the risk-based regulatory framework consistent with international standards. The capacity building will strengthen the ability of the examination teams to systematically review the insurance sector and monitor the activities of individual companies – from licensing to financial analysis. The Insurance Commissioner has also identified training requirements on (iii) supervision of self-regulating industry organizations; and (iv) training on ADR which will be considered as possible, by the TA.

## III. THE TECHNICAL ASSISTANCE

### A. Impact and Outcome

8. The impact of the TA will be: Improved supervisory functions in the Insurance Commission. The outcome will be: Recommendations on Risk-Based Capital (RBC) supervisory reporting.

### B. Methodology and Key Activities

9. **Output 1: IC staff training on risk-based capital requirements.** (i) Review the current surveillance and examination processes for the life, non-life and pre-need industry<sup>10</sup>; support the forensic investigation of companies that need to be consolidated / liquidated; (ii) build on the "screen based" early warning system supporting risk based analysis for life insurance, and consider the potential to extend to other insurance sub-sectors; (iii) review the workflow in office/

<sup>7</sup> Expiry date will be December 31; Renewable every 3 years.

<sup>8</sup> The Commissioner will require the adoption of the risk-based capital approach and other internationally accepted forms of capital framework. Net worth shall consist of: Paid-up capital; Retained earnings; Unimpaired surplus; and Revaluation of assets as may be approved by the Commissioner.

<sup>9</sup> Capitalization requirements set forth in the new Insurance Code are as follows: P250.0 million in 2013; P550.0 million in 2016; P900.0 million in 2019, and P1.2 billion in 2022.

<sup>10</sup> The current processes are compliance rather than risk-based, as these institutions have recently been transferred from the SEC to the IC and not all necessarily comply yet with legislation.

off-site investigations and assess the process of resource intensive on-site examinations; (iv) assess staff skills in surveillance especially, actuarial reserves and risk based capital; (v) in coordination with an international training center, upgrade capacity on solvency requirements consistent with international standards. Consider additional training on anti-money laundering, corporate governance and fair claim settlement practices, including ADR.

10. **Output 2: Upgrade IT to support the risk-based regulatory framework.** The scope of work will require an (i) assessment of the existing regulatory reports; (ii) review potential changes to report contents as per solvency requirements consistent with international standards; (iii) assess the existing process for capturing, validating, and publishing supervisory data; and (iv) evaluate existing IT capabilities to build consensus between the IC and the non-life insurance companies, on the best way to automate returns. The TA will (v) diagnose the required upgrades (2 weeks); (vi) design the upgrades and pilot test the new system (3 months); (vii) review pilot results and refine the IT system; and (viii) initiate system roll-out (4 – 6 months) in close coordination with the Insurance Commission's IT Manager and division team.

### C. Cost and Financing

11. The total cost of the TA is estimated to be \$225,000 to be funded under the Technical Assistance Special Fund (TASF) (Appendix 2). The government will provide counterpart support in the form of office accommodation and transport.

### D. Implementation Arrangements

12. The Insurance Commission will be the executing agency and the Public Management, Financial Sector, and Trade Division (SEPF) within the Southeast Asia Department, will be the focal point.<sup>11</sup> One international consultant (total of 30 person-days) will be recruited by the ADB on an individual, lump-sum basis, to provide on-site training in examination and, in consultation with the Insurance Commission, identify an international training center program that will provide on-site, customized training, at the IC. The international training centre will be hired on a lump-sum basis. Another international consultant will be hired on an individual basis, lump-sum, to review and develop the framework for IT upgrading (total of 70 days). Consultants will be engaged in accordance with ADB's *Guidelines on the Use of Consultants* [2010 as amended from time to time]. Disbursements under the TA will be made in accordance with the ADB's *Technical Assistance Disbursement Handbook* (2010, as amended from time to time). The TA will commence on 7 January 2014 and will be completed 30 September 2014. The consultants' terms of references are attached as Appendix 3.

### E. Preliminary Risk Assessment

13. Overall, risk is considered low as the focus of the TA will be limited to identifying the gaps in staff examination skills and IT processes. The TA has the strong support of the Insurance Commissioner and the four Deputy Commissioners which will facilitate the sustainable implementation of agreed upgraded processes in the Insurance Commission.

<sup>11</sup> No activity, financed by ADB shall commence in the territory of any of the participating countries unless a no objection letter is obtained, in writing, from the government of that participating country.

#### IV. RECOMMENDATION

14. Pursuant to the authority delegated to heads of departments and offices to approve small-scale technical assistance, your approval is requested to provide a small-scale capacity development technical assistance to support completion of an IT Upgrading at the Insurance Commission - Supporting Regulation and Oversight in an amount not exceeding the equivalent of \$225,000 on a grant basis from the Technical Assistance Special Fund (TASF)

15. Such approval will be reported to the Board in the Quarterly Summary Report on Small-Scale and Supplementary Technical Assistance Projects not exceeding \$225,000.

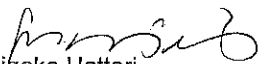
cc: Vice President (Operations 2); Assistant General Counsel, OGC; Assistant Controller, CTLA; Directors, OSP2, OCO, RSGS; Country Director, PhCO; Senior Advisor to VPO2 (S. Shrestha); R. Bolt/S. Tukuafu/E. Thomas; Country Team Leader/PAU Head, SEPF; Project File



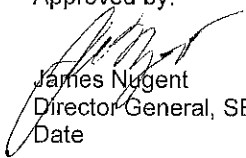
## DESIGN AND MONITORING FRAMEWORK

Design Summary	Performance Targets/Indicators	Data Sources/Reporting Mechanisms	Assumptions and Risks
<b>Impact</b> Improved supervisory functions in the Insurance Commission.	By 2016, the average examination review period is shortened.  Proxy measure: the review period is shortened from 6 months to 4 months.	Insurance Commission Website	<b>Risk</b> Existing inefficiencies may benefit vested interests which could result in strong resistance to change.  <b>Assumption</b> The IC continues to receive the strong support of the Department of Finance Secretary to implement reforms.
<b>Outcome</b> Recommendations on Risk-Based Capital supervisory reporting	By December 2014, the consultants' report identifies areas of improved IC staff expertise.	ADB website  TA consultants' reports	
<b>Output</b> 1. IC staff training on risk-based capital examinations is accepted and implemented.  2. IT framework is developed and implemented	Training content and milestones identified in the consultant's report.  IT specifications, procedures and timelines are identified in the consultant's report.	IC Reports TA consultants' reports	
<b>Activities with Milestones</b>  1. IC staff training on risk-based capital examinations is accepted and implemented 1.1 Initiate site visit (January 2014) by international experts 1.2 Training timelines by major area of examination are identified in the consultants' report and submitted to the IC (end-January 2014) 1.3. International training experts initiate training at the IC (February 2014) 1.4. Final report completed and published on ADB website (end-November 2014)  2.0 IT diagnostic framework is developed and implemented 2.1 Initiate site visit (January 2014) 2.2 Timelines and procedures to update the IT is identified in the consultant's mid-term report and submitted to the IC (end-March 2014) 2.3. Pilot implementation (May 2014) 2.4. System roll-out (September-October 2014) 2.5 Final report completed and published on ADB website (December 2014)			<b>Inputs</b>  ADB TA of \$225,000 funded under Technical Assistance Special Fund (TASF) allocated among: <ul style="list-style-type: none"> <li>• International consultants' fees and travel expenses \$160,000</li> <li>• Additional international training of selected IC staff at a relevant supervisory training center: \$30,000</li> <li>• Workshops: \$25,000</li> <li>• Reports &amp; Communications \$5,000</li> <li>• Contingency \$5,000.</li> <li>• The government will provide counterpart support in the form of office accommodation and transport.</li> </ul>

Endorsed by:

  
Shigeko Hattori  
Director, SEPF  
Date:

Approved by:

  
James Nugent  
Director General, SERD  
Date





**COST ESTIMATES AND FINANCING PLAN**  
(\$ 000)

<b>Item</b>	<b>Total Cost</b>
<b>A. Asian Development Bank Financing</b>	
1. Consultants	
a. Remuneration and Per Diem	
i. International Consultants	150.00
b. International and Local Travel	10.00
2. International training of IC staff at a regional supervisory training centre	30.00
3. Workshops, Training, Seminars, and Conferences	25.00
4. Report and Communication	5.00
5. Contingencies	5.00
<b>Total</b>	<b>225.00</b>

Source: Asian Development Bank estimates.

Source of Funding: Technical Assistance Special Fund (TASF) V

Note 1: The budget for the workshops, training, seminars and conferences will be administered by the TA consultants (refer to consultants' TOR).

Note 2: Advances provided for workshops, trainings, seminars and conferences will be liquidated within a 30-day period, to ensure that the TA can be closed in a timely manner.

Note 3: The government will provide counterpart support in the form of office accommodation and transport



## TERMS OF REFERENCE

### I. International Risk-Based Supervision and Examination Experts (Insurance)

#### A. Objective of the Assignment

1. The objective of this assignment is to identify the training requirements of existing and incoming IC staff on surveillance and examination processes for the life, non-life and pre-need industry – particularly in the area of actuarial reserves and risk based capital as per international standards. As possible, also consider training on anti-money laundering requirements, good corporate governance and fair claim settlement practices.

#### B. Minimum Qualifications

2. The experts, individuals or members of an insurance or actuarial consultancy, should have 10 years senior experience in the insurance industry and knowledge of the regulatory and supervisory standards in the Asia Pacific region. The experts will also have experience in international benchmarking and training exercises covering insurance supervision. The project is located in the Philippines and will require the experts to coordinate with / or draw upon training on risk-based capital solvency and supervision from supervisory training centres in the Republic of South Korea, Malaysia, Singapore, Hong Kong (China), or the OECD member countries - held in coordination with or sponsored by the National Association for Insurance Commissioners of the US and / or the International Association of Insurance Supervisors - for training assessment, coordination and identification as per the requirements of the Insurance Commission. The scope of work will include the following:

#### C. Scope of Work:

##### Phase I

- (i) Review and summarize existing staff complements and skills in the area of insurance examination.
- (ii) In conjunction with the Insurance Commissioner and the Deputy Commissioners, develop a comprehensive and comparable training guideline for IC staff on, and by order of priority: actuarial reserves and risk-based capital; and as possible, anti-money laundering requirements, good corporate governance and fair claim settlement practices as well as enterprise risk management.
- (iii) Initiate and administer the workshops and seminars within TA budget – as per agreed specifications with the Insurance Commission and ADB.

##### Phase II

- (iv) Identify training timelines in the priority areas identified above, and identify the costs within the TA training budget for on-site training in the Philippines.
- (v) Together with the Insurance Commissioner and the Deputy Commissioners, and in consultation with ADB, develop a competitive selection criteria whereby Insurance Commission staff are ranked for in-house training on the basis of knowledge and performance. Develop a recognition award for graduated staff.
- (vi) Provide regular briefing reports on training results undertaken at the at the Insurance Commission, and make recommendations for training adjustment, as may be required.

- (vii) Based on merit, shortlist IC staff for additional international training, at the most relevant regional supervisory training centre, in one or more of the following areas: actuarial reserves and risk-based capital; anti-money laundering, good corporate governance and fair claim settlement practices as well as enterprise risk management.

#### **D. Output/Report Requirements**

3. The consultancy will require up to 40 working days of experts, individuals or members of an insurance or actuarial consultancy, to commence in January 2014. The experts will document the scope and specific nature of required skills upgrading in the area of examination and submit the report for consideration by the Insurance Commission and ADB. The insurance / actuarial experts will have a track record in training insurance supervisors in the Asia-Pacific region and will provide the training of Insurance Commission staff as per the criteria reviewed and approved by the Insurance Commission and ADB.

#### **E. Deliverables**

4. The experts will diagnose the scope and depth of training required at the Insurance Commission, prepare an inception report communicating the findings of the review, including an analysis of training requirements, costs and a summary explanation, to the extent possible, of any significant differences in examination standards in comparative markets. The final report will document the scope of training provided by the experts in the Philippines, and make recommendations for selected staff training at a relevant regional training centre. The experts will also assess the specific areas for additional training and provide recommendations, as may be required, in the final report.

### **II. International IT and Supervisory Reporting Expert (Banking and Insurance)**

#### **F. Objective of the Assignment**

5. The objective of this assignment is to review the existing system for capturing, validating, consolidating and publishing supervisory data relative to the existing IT capabilities at the Insurance Commission, and identify changes to supervisory returns as well as implement upgraded IT-based forms.

#### **G. Minimum Qualifications**

6. The expert should have more than 15 years senior experience in the banking and insurance industry on developing customized, and sustainable solutions in process and IT internationally – in transition and middle income countries. The expert will also have experience in international benchmarking covering process and IT preferably with a recognized international management consulting firm(s). The project is located in the Philippines. The scope of work will include the following:

#### **H. Scope of Work:**

##### **Phase I**

- (i) Review existing regulatory reports and identify scope of upgrading in consultation with the Insurance Commissioner and the Deputy Commissioners

- (ii) In conjunction with the Insurance Commissioner and the Deputy Commissioners, identify and agree on changes to supervisory returns and build consensus on best way to automate returns in the short-term.
- (iii) Initiate and administer the workshops and seminars within TA budget – as per agreed specifications with the Insurance Commission and ADB.

#### Phase II

- (iv) Document any required changes to the manual system
- (v) Document key IT capabilities required to implement
- (vi) Develop implementation plan for short and medium-term
- (vii) Build consensus and reach agreement to proceed with the Insurance Commission and ADB
- (viii) Implement short-term automation of regulatory returns further to pilot testing
- (ix) Implement system roll-out within available TA budget
- (x) Identify additional resources as may be required.

#### **I. Output/Report Requirements**

7. The consultancy will require a total of 70 working days of an international consultant to commence in January 2014. The expert will undertake Phase I implementation over the January – end-March 2014 period. Thereafter, in coordination and further to the agreement of the Insurance Commissioner, the expert will (a) undertake Phase II implementation within the specified timelines of Phase II deliverables referenced above (iv and v); (b) diagnose the required upgrades (within 2 weeks); (c) design the upgrades and pilot test the new system (within 3 months); (d) review pilot results and refine the IT system (within 3 months); and (e) initiate system roll-out (within 4 – 6 months) in close coordination with the Insurance Commission's IT Manager and division team. The expert will be based in the Philippines.

#### **J. Deliverables**

8. Over a 9 month period, on an intermittent basis, the consultant will: (1) diagnose the required upgrades, (ii) design the upgrades and pilot test the new system within 3 months, (iii) review the results of the pilot and refine the IT system as required, and (iv) initiate basic system roll-out within 4-6 months, as practicable within the TA budget.

9. The expert will prepare a mid-term report communicating the findings of the review, pilot implementation, and the requirements to implement system roll-out, including an analysis of the IT requirements, costs and a summary explanation based on relevant regional and / or international comparators. The final report will document further requirements for system upgrading in the medium-term, as may be warranted.