Alberta Treasury Board and Finance

Financial Sector Regulation and Policy
Superintendent of Insurance
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December 9, 2014

To All Insurance Entities Supervised by the Alberta Superintendent of Insurance (“Superintendent”), including (collectively defined as “Provincially Regulated Insurance Entities”):

- Provincially Incorporated Property & Casualty Insurance Companies;
- Provincially Incorporated Life Insurance Companies;
- Reciprocal Insurance Exchanges either formed under the *Insurance Act* or who have transferred to Alberta such that Alberta is their primary regulator; and
- Applicable Exempt Entities.

Section 414 of the *Insurance Act* (“Act”) requires Provincially Regulated Insurance Entities to maintain adequate capital. The Minimum Capital Test (“MCT”) and Minimum Continuing Capital and Surplus Requirements (“MCCSR”) ratios are two of several indicators that the Superintendent uses to assess a Provincially Regulated Insurance Entity’s financial condition and capital adequacy, depending on the classes of insurance for which an entity is licensed.

Effective January 1, 2015, the Superintendent will enforce the new Guidelines for these two ratios. With the conversion to the new Guidelines, there are a number of items that require further explanation to ensure clarity of the Superintendent’s expectations:

- For the 2014 annual return based on the fiscal year ended December 31, 2014, the Provincially Regulated Insurance Entities must file their return under the Guideline effective January 1, 2013.

- For the 2015 annual return based on the fiscal year ended December 31, 2015, the Provincially Regulated Insurance Entities must file the current and prior years in the 2015 return under the Guideline effective January 1, 2015.
- Contrary to the Guidelines, the Audit Report on the MCT and MCCSR is due within 60 days after the fiscal year-end for Provincially Incorporated Insurance Companies and by the last day of February after the fiscal year-end for Reciprocal Insurance Exchanges supervised by the Superintendent.

MCT

- Provincially Regulated Insurance Entities held to the MCT are required to phase-in the capital impact of the revised Guideline, regardless of whether the entity is affected positively or negatively by the adjustments, to ensure that all entities are treated equally. As such, the entity must calculate the MCT under the Guideline effective January 1, 2015 for the fiscal year ended December 31, 2014. Contrary to the Guideline, this additional calculation must be filed with the Superintendent in the form of a separate submission of the MCT pages 30.70 – 30.73 in Excel format through the 2015 (Q1) Sample Return.
- For Provincially Regulated Insurance Entities that are required to file the MCT on a quarterly basis, the capital impact of the revised Guideline must be phased-in over twelve quarters, starting with the first quarter ending in 2015. The phase-in values must be calculated using the following formulae:

  Phase-in Capital Available *=*

  $$A - (n/12)(B - C)$$

  Where

  A is defined as the Capital Available under the 2015 MCT for the applicable quarter;

  B is defined as the Capital Available under the 2015 MCT at December 31, 2014;

  C is defined as the Capital Available under the 2013 MCT at December 31, 2014; and

  n is defined as the applicable quarter in the twelve month phase-in period, declining from 11 in the first quarter 2015 to 0 in the fourth quarter 2017.

  Phase-in Capital Required =

  $$A - (n/12)(B - C)$$

  Where

  A is defined as the Capital Required under the 2015 MCT for the applicable quarter;

  B is defined as the Capital Required under the 2015 MCT at December 31, 2014;

  C is defined as the Capital Required under the 2013 MCT at December 31, 2014; and

  n is defined as the applicable quarter in the twelve month phase-in period, declining from 11 in the first quarter 2015 to 0 in the fourth quarter 2017.

- For Provincially Regulated Insurance Entities that are required to file the MCT on an annual basis, the capital impact of the revised Guideline must be phased-in over three years, starting with the first year ending in 2015. The phase-in values must be calculated using the following formulae:

  Phase-in Capital Available *=*

  $$A - (n/3)(B - C)$$

Where

A is defined as the Capital Available under the 2015 MCT for the applicable annual;

B is defined as the Capital Available under the 2015 MCT at December 31, 2014;

C is defined as the Capital Available under the 2013 MCT at December 31, 2014; and

n is defined as the applicable quarter in the 3 year phase-in period, declining from 2 in the first annual 2015 to 0 in the third annual 2017.

***Phase-in Capital Required** =*

$$A - \left(n/3\right)\left(B - C\right)$$

Where

A is defined as the Capital Available under the 2015 MCT for the applicable annual;

B is defined as the Capital Available under the 2015 MCT at December 31, 2014;

C is defined as the Capital Available under the 2013 MCT at December 31, 2014; and

n is defined as the applicable quarter in the 3 year phase-in period, declining from 2 in the first annual 2015 to 0 in the third annual 2017.

- For Provincially Regulated Insurance Entities that file the MCT on a monthly basis, the capital impact of the revised Guideline must be phased-in over thirty six months, starting with the first month ending in January 2015. The formulae detailed above would still apply, with the appropriate adjustments.

MCCSR

- It should be noted that the phase-in requirement is not necessary for the MCCSR Guideline effective January 1, 2015; therefore, the adjustments based on the adoption of the new Guideline should be incorporated in the first quarter of 2015.

Provincially Regulated Insurance Entities are required to inform the Superintendent immediately if they anticipate falling below their Internal Target, which must include a detailed outline of their plans to return to their Internal Target for the Superintendent's supervisory approval. The Superintendent will consider any unusual conditions in the market environment when evaluating the entity's performance against their Internal Target.

Should you have any questions about the Superintendent's expectations surrounding the transition to the new Guidelines, please feel free to contact us directly by telephone at 780-415-6496 or by e-mail to tbf.insurance-licens@gov.ab.ca.

Sincerely,

[ORIGINAL SIGNED]

Prudential Supervision