

## **GRF\_116\_0\_G: Insurance Concentration Risk Charge (G)**

These instructions must be read in conjunction with the general instruction guide.

### **Explanatory notes**

#### **Insurance concentration risk charge (ICRC)**

The Level 2 insurance group is not required to report each component of the ICRC where the amount determined for one or more of the components is always expected to be materially lower than the amount determined for one or more of the other components.

#### **Natural perils horizontal requirement (NP HR)**

The NP HR of the ICRC will be effective from 1 January 2014.

This would mean that, from 1 January 2013 to 31 December 2013, the calculation of ICRC will be based only on the natural perils vertical requirement (NP VR), the other accumulations vertical requirement (OA VR) and the lenders mortgage insurer concentration risk charge (LMICRC). The NP HR must be considered for calculating the ICRC for reporting periods commencing after 1 January 2014.

### **Instructions for specific items**

#### **Region/Approach**

The Level 2 insurance group must enter the region used to determine the applicable component that produces the highest ICRC. Where the Level 2 insurance group has used an approach agreed with APRA under paragraph 7(b) of Attachment B of *Prudential Standard GPS 116 Capital Adequacy: Insurance Concentration Risk Charge* (GPS 116), enter 'APRA-agreed approach' in this field.

#### **1. Natural perils vertical requirement (NP VR)**

The NP VR is automatically calculated as:

- (a) the greater of Item 1.2 less Item 1.3, or Item 1.4; less
- (b) Item 1.5; plus
- (c) Item 1.6; less
- (d) Item 1.7.

### **1.1 Basis for determination of NP VR**

The Level 2 insurance group must enter 'Gross' or 'Net' at this item.

The Level 2 insurance group must enter 'Gross' if it has determined that the NP VR would be greater, if it is based on the gross loss arising from the occurrence of a single event, than the net loss arising from the occurrence of a single event.

The Level 2 insurance group must enter 'Net' if it has determined that the NP VR would be greater, if it is based on the net loss arising from the occurrence of a single event, than the gross loss arising from the occurrence of a single event.

### **1.2 NP PML**

The Level 2 insurance group must only report this item if the Level 2 insurance group has entered 'Gross' in Item 1.1.

NP PML is the gross loss arising from the occurrence of a single event, where that loss is not less than the whole-of-portfolio annual loss with a 0.5 per cent probability of occurrence.

### **1.3 Less: NP reinsurance recoverables**

The Level 2 insurance group must only report this item if the Level 2 insurance group has entered 'Gross' in Item 1.1.

NP reinsurance recoverables is the level of potential reinsurance recoverables should there be the occurrence of the event that gives rise to NP PML. This amount must not include any amounts due from aggregate reinsurance cover.

### **1.4 Net whole-of-portfolio loss**

The Level 2 insurance group must only report this item if the Level 2 insurance group has entered 'Net' in Item 1.1.

Net whole-of-portfolio loss is the net loss arising from the occurrence of a single event where that net loss is not less than the whole-of-portfolio annual net loss with a 0.5 per cent probability of occurrence.

### **1.5 Less: NP reinstatement premiums**

NP reinstatement premiums are applicable to Level 2 insurance groups that write reinsurance and may receive inwards reinstatement premiums from cedants as a result of the event that gives rise to its NP PML, or the net whole-of-portfolio loss. NP reinstatement premiums must only be included in NP VR if the reinsurance contract specifically stipulates that offsetting with the cedant will occur at the time of the payment of the reinsurance claim.

### **1.6 Add: NP reinstatement cost**

NP reinstatement cost is the cost (if any) of reinstating all catastrophe reinsurance cover relating to the reinsurance recoverables determined. In determining this cost, if

the Level 2 insurance group does not have contractually agreed rates for the reinsurance cover, the Level 2 insurance group must estimate the cost based on current reinsurance market conditions. The amount must not be less than the full original cost of the cover with no deduction for the expiry of time since the inception of the reinsurance arrangements unless the Level 2 insurance group is able to demonstrate to APRA that the amount materially overstates the cost that would prevail.

### **1.7 Less: Other adjustments**

Other adjustments include potential reinsurance recoverables from aggregate reinsurance cover. Aggregate reinsurance cover is eligible to be considered for inclusion in the NP VR once the aggregate reinsurance cover has reached its attachment point, or will as a result of the occurrence of NP PML, or net whole-of-portfolio loss, as appropriate. The reinsurance recoverables from aggregate reinsurance cover must then be applied up until the cover has been exhausted by claims by the Level 2 insurance group or the date that the aggregate reinsurance treaty expires, whichever occurs first.

## **2. Natural perils horizontal requirement (NP HR)**

The NP HR is automatically calculated by the form and is equal to the greater of Items 2.3 and 2.4, less Item 2.5.

### **2.1 Commencement date of catastrophe reinsurance program**

The Level 2 insurance group is required to report the commencement date of the catastrophe reinsurance program. Where the Level 2 insurance group has multiple inception dates for its catastrophe reinsurance program it must consult with APRA to determine the relevant commencement date.

### **2.2 End date of catastrophe reinsurance program**

The Level 2 insurance group is required to report the end date of the catastrophe reinsurance program. Where the Level 2 insurance group has multiple inception dates for its catastrophe reinsurance program it must consult with APRA to determine the relevant end date.

### **2.3 H3 requirement**

The H3 requirement is automatically calculated in this form as the sum of the determined amounts for the three events in Item 2.3.7.

#### **2.3.1 Basis for determination of H3 requirement**

The Level 2 insurance group must select 'Gross' or 'Net' from the drop-down box.

The Level 2 insurance group must select 'Gross' if it has determined that the H3 requirement would be greater if it is based on the gross loss arising from the occurrence of a single event, when compared to the net loss arising from the occurrence of a single event.

The Level 2 insurance group must select 'Net' if it has determined that the H3 requirement would be greater if it is based on the net loss arising from the occurrence of a single event, when compared to the gross loss arising from the occurrence of a single event.

### **2.3.2 Single event loss from H3 event**

The single event loss from the H3 event is the gross or net loss from the occurrence of a single event, where that loss is not less than the whole-of-portfolio annual (gross/net) loss with a 10 per cent probability of occurrence.

### **2.3.3 H3 reinsurance recoverables**

This item must only be reported if the Level 2 insurance group has selected 'Gross' in Item 2.3.1.

H3 reinsurance recoverables are the level of potential reinsurance recoverables should there be the occurrence of three H3 losses over the catastrophe reinsurance program treaty year. H3 reinsurance recoverables must not include any amounts due from aggregate reinsurance cover.

Column 4 is automatically calculated as the sum of Columns 1 to 3.

### **2.3.4 H3 aggregate offset**

H3 aggregate offset is the amount of potential reinsurance recoverables from aggregate reinsurance cover. The Level 2 insurance group must not allow for any reinstatements of aggregate reinsurance cover unless these have been contractually agreed with the reinsurer(s). If reinstatements are included, the cost of reinstatement must be netted from the offset. The Level 2 insurance group must agree with APRA a methodology for the determination of this adjustment.

This methodology may allow for any portion of paid and outstanding claims and premiums liabilities (PL) that contribute to the Level 2 insurance group's retained losses for the purposes of the retention on any aggregate reinsurance cover, provided it does not result in a double-count between this offset and the PL offset.

Column 4 is automatically calculated as the sum of Columns 1 to 3.

### **2.3.5 H3 reinstatement premiums**

H3 reinstatement premiums are applicable to Level 2 insurance groups that write reinsurance and may receive inwards reinstatement premiums from cedants as a result of the events that give rise to three H3 losses. H3 reinstatement premiums must only be included in NP HR if the reinsurance contract specifically stipulates that offsetting with the cedant will occur at the time of the payment of the reinsurance claim.

Column 4 is automatically calculated as the sum of Columns 1 to 3.

### **2.3.6 H3 reinstatement cost**

The Level 2 insurance group is not required to determine a H3 reinstatement cost after the third event.

NP reinstatement cost is the cost (if any) of reinstating catastrophe reinsurance cover after the occurrence of the first two H3 losses. The cost (if any) must reflect the cost of reinstating reinsurance cover up to the size of the third event. In determining this cost, if the Level 2 insurance group does not have contractually agreed rates for the reinsurance cover, the Level 2 insurance group must estimate the cost based on the reinsurance market conditions that would prevail after the occurrence of the events. The amount must not be less than the full original cost of the cover, with no deduction for the expiry of time since the inception of the reinsurance arrangements unless the Level 2 insurance group is able to demonstrate to APRA that the amount materially overstates the cost that would prevail in the market after the occurrence of the events.

Column 4 is automatically calculated as the sum of Columns 1 to 2.

### **2.3.7 H3 loss per event**

The H3 loss per event is automatically calculated by the form and is equal to Item 2.3.2 less Item 2.3.3 less Item 2.3.4 less Item 2.3.5 plus Item 2.3.6 (except for the third event). This is to be determined for each H3 event.

## **2.4 H4 requirement**

The H4 requirement is automatically calculated in this form as the sum of the determined amounts for the four events in Item 2.4.7.

### **2.4.1 Basis for determination of H4 requirement**

The Level 2 insurance group must select 'Gross' or 'Net' from the drop-down box.

The Level 2 insurance group must select 'Gross' if it has determined that the H4 requirement would be greater if it is based on the gross loss arising from the occurrence of a single event, when compared to the net loss arising from the occurrence of a single event.

The Level 2 insurance group must select 'Net' if it has determined that the H4 requirement would be greater if it is based on the net loss arising from the occurrence of a single event, when compared to the gross loss arising from the occurrence of a single event.

### **2.4.2 Single event loss from H4 event**

The single event loss from the H4 event is the gross or net loss from the occurrence of a single event, where that loss is not less than the whole-of-portfolio annual loss with a 16.7 per cent probability of occurrence.

### **2.4.3 H4 reinsurance recoverables**

This item must only be reported if the Level 2 insurance group has selected 'Gross' in Item 2.4.1.

H4 reinsurance recoverables are the level of potential reinsurance recoverables should there be the occurrence of four H4 losses over the catastrophe reinsurance program treaty year. H4 reinsurance recoverables must not include any amounts due from aggregate reinsurance cover.

Column 5 is automatically calculated as the sum of Columns 1 to 4.

### **2.4.4 H4 aggregate offset**

H4 aggregate offset is the amount of potential reinsurance recoverables from aggregate reinsurance cover. The Level 2 insurance group must not allow for any reinstatements of aggregate reinsurance cover unless these have been contractually agreed with the reinsurer(s). If reinstatements are included, the cost of reinstatement must be netted from the offset. The Level 2 insurance group must agree with APRA a methodology for the determination of this adjustment.

This methodology may allow for any portion of paid and outstanding claims and PL that contribute to the Level 2 insurance group's retained losses for the purposes of the retention on any aggregate reinsurance cover, provided it does not result in a double-count between this offset and the PL offset.

Column 5 is automatically calculated as the sum of Columns 1 to 4.

### **2.4.5 H4 reinstatement premiums**

H4 reinstatement premiums are applicable to Level 2 insurance groups that write reinsurance and may receive inwards reinstatement premiums from cedants as a result of the events that give rise to three H4 losses. H4 reinstatement premiums must only be included in NP HR if the reinsurance contract specifically stipulates that offsetting with the cedant will occur at the time of the payment of the reinsurance claim.

Column 5 is automatically calculated as the sum of Columns 1 to 4.

### **2.4.6 H4 reinstatement cost**

The Level 2 insurance group is not required to determine a H4 reinstatement cost after the fourth event.

H4 reinstatement cost is the cost (if any) of reinstating catastrophe reinsurance cover after the occurrence of the first three H4 losses. The cost (if any) must reflect the cost of reinstating reinsurance cover up to the size of the fourth event. In determining this cost, if the Level 2 insurance group does not have contractually agreed rates for the reinsurance cover, the Level 2 insurance group must estimate the cost based on the reinsurance market conditions that would prevail after the occurrence of the events. The amount must not be less than the full original cost of the cover, with no deduction for the expiry of time since the inception of the reinsurance arrangements unless the

Level 2 insurance group is able to demonstrate to APRA that the amount materially overstates the cost that would prevail in the market after the occurrence of the events.

Column 5 is automatically calculated as the sum of Columns 1 to 3.

#### **2.4.7 H4 loss per event**

The H4 loss per event is automatically calculated by the form and is equal to Item 2.4.2 less Item 2.4.3 less Item 2.4.4 less Item 2.4.5 plus Item 2.4.6 (except for the fourth event). This is to be determined for each H4 event.

### **2.5 PL offset**

‘PL offset’ is the portion of the premiums liability provision which relates to catastrophic losses (those that give rise to a relatively significant number of claims and occur no more frequently than every three months), as determined by the Group Actuary.

### **3. Other accumulations vertical requirement (OA VR)**

The OA VR is automatically calculated by this form as Item 3.1 less Item 3.2 less Item 3.3 plus Item 3.4.

#### **3.1 OA PML**

OA PML is the gross loss arising from the occurrence of a single event, where that loss has 0.5 per cent probability of occurrence over 12 months. A Level 2 insurance group with exposures to accumulations of losses arising from a common dependent source or non-natural perils must determine OA PML.

#### **3.2 Less: PL adjustment to OA PML**

The Level 2 insurance group may reduce the OA PML for any losses included in the other accumulation scenario that is already specifically allowed for in the PL of the Level 2 insurance group.

#### **3.3 Less: OA reinsurance recoverables**

OA reinsurance recoverables is the level of potential reinsurance recoverables should there be occurrence of OA PML. This amount may include any amounts from aggregate reinsurance cover if the cover has reached its attachment point, or will as a result of OA PML.

The reinsurance recoverables can then be applied until the cover has been exhausted by claims by the Level 2 insurance group or the date that the aggregate reinsurance treaty expires, whichever occurs first.

#### **3.4 Add: OA reinstatement cost**

OA reinstatement cost is the cost (if any) of reinstating all catastrophe reinsurance cover relating to OA reinsurance recoverables. In determining this cost, if the Level 2 insurance group does not have contractually agreed rates for the reinsurance cover, the

Level 2 insurance group must estimate the cost based on the current reinsurance market conditions. The amount must not be less than the full original cost of the cover with no deduction for the expiry of time since the inception of the reinsurance arrangements unless the Level 2 insurance group is able to demonstrate to APRA that the amount materially overstates the cost that would prevail.

#### **4. LMI Concentration Risk Charge (LMICRC)**

This is automatically calculated as the greater of 10 per cent of Item 4.3 or, Item 4.6 less Item 4.7 plus Item 4.8.

The LMICRC is subject to a floor of 10 per cent of adjusted PML.

#### **PML Year 1**

This represents the years for the Prescribed Stress Scenario which is in the form of a three-year economic or property downturn. The PML is allocated in the proportion of 25 per cent to year one, 50 per cent to year two and 25 per cent to year three of the downturn.

##### **4.1 PML**

PML represents the total PML across all loan types, coverage types and origination channels. The Level 2 insurance group must enter an amount for Total PML. Total PML is then automatically allocated in the proportions of 25 per cent to year one, 50 per cent to year two and 25 per cent to year three of the Prescribed Stress Scenario.

##### **4.2 Adjustment to the PML**

For a Level 2 insurance group with an LMI that is no longer writing new business (i.e. in run-off), the sum insured is expected to decrease over the three-year scenario and it may be appropriate for an LMI in run-off to adjust its PML downwards. The methodology for adjusting an LMI's PML in a run-off situation must be approved by APRA and documented in the LMI's Reinsurance Management Strategy.

A reduction in PML is to be entered as a positive amount. Do not enter any other adjustments to PML in this field.

##### **4.3 Adjusted PML**

This is automatically calculated as Item 4.1 less Item 4.2.

##### **4.4 Available reinsurance**

Report the amount of available reinsurance for each of the three years of the Prescribed Stress Scenario. The methodology for calculating available reinsurance is detailed in Attachment A of GPS 116.

##### **4.5 Allowable reinsurance**

This is the lesser of available reinsurance and 60 per cent of the adjusted PML. It is automatically calculated by the form.



#### **4.6 PML net of reinsurance**

This is automatically calculated as Item 4.3 less Item 4.5.

#### **4.7 Net premium liability deduction**

In determining the LMICRC, this is the value of the deduction from the PML, allowed under GPS 116, for net PL of the LMI that relate to an economic downturn.

It is to be reported as a positive amount.

#### **4.8 Adjustments to LMICRC as approved by APRA**

If APRA is of the view that the Standard Method for calculating the LMICRC component of the prescribed capital amount does not produce an appropriate outcome in respect of a Level 2 insurance group, or a Level 2 insurance group has used inappropriate judgement or estimation in calculating the LMICRC, APRA may adjust the LMICRC calculation for that Level 2 insurance group.

An increase in the LMICRC is to be reported as a positive amount.

### **5. Adjustments to Insurance Concentration Risk Charge**

If APRA is of the view that the Standard Method for calculating the ICRC component of the prescribed capital amount does not produce an appropriate outcome in respect of a Level 2 insurance group, or a Level 2 insurance group has used inappropriate judgement or estimation in calculating the ICRC, APRA may adjust the ICRC calculation for that Level 2 insurance group.

Approved adjustments are to be reported separately in the associated table highlighting the description of the adjustment given, transitional status and amount of adjustment applied. An increase in the risk charge is to be reported as a positive amount.

This is calculated automatically as the sum of Column 3.

### **6. Insurance Concentration Risk Charge**

This is automatically calculated by the form as the greater of Items 1 to 4, plus Item 5.