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FINSAC Annual Report 1999: Intervention & Rehabilitation - Insurance

Financial Sector Adjustment Company (Jamaica: FINSAC)

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FINSAC ANNUAL REPORT 1999

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Intervention & Rehabilitation - Insurance

The Insurance Intervention & Rehabilitation department is responsible for the restructuring, monitoring and rehabilitation of FINSAC intervened insurance companies. The companies are Crown Eagle Life Insurance Company Limited (Crown Eagle), Dyoll Life Limited (Dyoll Life), the Jamaica Mutual Life Assurance Society (Mutual Life), Island Life Insurance Company Limited (Island Life), and Life of Jamaica Limited (LOJ). FINSAC originally intervened in the insurance sector in fiscal 1997/98 through the purchase of common and preferred shares and/or subordinated loans in all five insurance companies. In 1998/99 it became evident that further intervention would need to take place in Crown Eagle, Dyoll Life and Mutual Life.

These companies were coming under increasing liquidity pressure from policyholders encashing their interest sensitive policies. It should be clearly stated that it has been FINSAC's view from the outset that these interest-sensitive investment-type policies do have a place in the insurance sector, provided they are segregated from the general fund, and provided they are properly matched with appropriate assets. Unfortunately, neither of these provisions were followed by Dyoll Life, Crown Eagle or Mutual Life. Consequently, viable arrangements for these portfolios needed to be made. In December 1998, FINSAC transferred all Dyoll Life policyholder liabilities to Crown Eagle. At the same time a new company - Independent Life Insurance Company (Independent Life) was formed as a platform for integrating the traditional life, and equity-linked portfolios of all the companies.

In order to manage this process, a consultant from the United States, who had had extensive experience working with troubled insurance companies, was appointed as Chief Executive Officer.

Court injunctions were also sought and obtained preventing Dyoll Life, Crown Eagle and Mutual Life from making any more payments on their interest-sensitive policies until February 11, 1999. In January 1999, an Emergency Fund was set up by FINSAC to allow interest-sensitive policyholders who could establish hardship and extreme need to obtain advance funds from their policies. This fund had paid approximately \$25 Million to some 2,000 policyholders as at June 25, 1999. In February, a Judicial Manager was appointed by the Courts to report on these interest-sensitive policies.

A scheme was also negotiated to transfer the proceeds of lump-sum type policies to the Bank of Nova Scotia (BNS). Under this scheme, policyholders would receive a savings account at BNS for their investment portion up to a \$200,000 maximum. Those with amounts over \$200,000 would be given a transferrable Certificate of Participation issued by ScotiaBank Jamaica Trust and Merchant Bank Limited (Scotia Trust), for the amounts over \$200,000. This Certificate in turn would be backed by a seven year term instrument issued by the Government of Jamaica with Scotia Trust as trustees.

Interest is payable semi-annually to these policyholders, but no withdrawal of principal is permitted during the seven years. Policyholders over 65 years old can receive interest monthly. This scheme gave approximately 75% of interest-sensitive policyholders immediate access to their funds. The cost is estimated to be \$2.4 Billion. (Subsequently, the term of the Certificates has been lowered to five years.) February

1999 also saw a second step towards FINSAC's divestment of its insurance portfolio holdings. Whilst rigorous analysis had shown that the combination of traditional and equity-linked portfolios would make Independent Life extremely viable with appropriate management, FINSAC had continued to look closely into the existing insurance companies, expecting to find additional unpleasant surprises.

Not only was this not the case, but other players in the insurance market were indicating that there could be considerable interest in the portfolios FINSAC controlled. In mid February, after weighing the options, FINSAC decided to offer the remaining Dyoll Life, Mutual Life and Crown Eagle portfolios for sale. If satisfactory offers were received, the advantages would be:

- Removal of risk - Government does not need to assume risk if the market itself will
- Removal of the need to establish the operational administration for Independent Life
- Early introduction of private sector capital, management practices and incentives
- Possible early divestment of some FINSAC non-financial asset holdings to underwrite the portfolios
- Accelerated divestment mitigates the unjustified perception that FINSAC holds on to institutions too long.

Actuarial evaluations of the portfolios took place, and by the end of March, eight life insurance companies from Jamaica and other Caribbean countries had submitted bids. The valuation was conducted in three stages: the group insurance (including health) business, the pension business and the individual life business. Based on several scenarios and assumptions, the reports provided a range of appraisal values for the portfolios as well as the value of the policy liabilities and the required capital. The reports also assumed a model asset portfolio appropriate for each liability class, consisting of real estate, equities, policy loans, long-term bonds and treasury bills.

As each stage of the valuation was completed, the valuation reports were passed on to the bidders, who were given a fixed time period to assess the portfolio and submit a bid on that portion of the business. The companies could submit bids for a portion or all of the portfolios, and could make their bids contingent on a successful tender for other segments of the portfolios.

Due to this feature of the bid process, the portfolios could be awarded to one company or a combination of companies. The criteria used to evaluate the bidders were:

- The potential owner be a fit and proper entity to operate a company of this nature
- The potential owner of the portfolios have the financial capacity to acquire and operate the business
- The potential owner of the portfolio have managerial capability specific to the life insurance or health insurance industry as evidenced by historical performance and the operating and business plans submitted
- The bid price.

On May 19, 1999, it was announced that Guardian Holdings Limited of Trinidad had won the bid for the individual life and pension portfolios and that a Jamaican company, First Life, had won the bid for the group life and health portfolios. The total price was J\$1.3 Billion. Upon completion of the diligence process and the necessary approvals of the Court, the portfolios will be transferred to the successful bidders.

IADB PROJECT

Throughout fiscal 1998/1998, Insurance Regulatory Reform has continued to be a major work stream through a two-year special project jointly funded by FINSAC and the Washington-based Inter-American Development Bank (IADB). This project has been specifically geared towards the management of FINSAC's investment in the insurance sector, the updating and strengthening of Jamaica's Insurance Act and regulations, the evaluation of the management of private pension funds in Jamaica, together with other reforms.

The project team is led by FINSAC's General Manager, Intervention & Rehabilitation - Insurance. The team works closely with the Office of the Superintendent of Insurance (OSI) to ensure their training and support in the new methodologies.

The following deliverables have been successfully completed:

- Performance benchmarks (Early Warning Ratios) established for FINSAC intervened insurance companies
- Monthly reporting forms for life and general insurance companies. These are now used by all FINSAC intervened insurance companies.
- A report on all life and general insurance companies, showing the trends in the predictive ratios over a nine year completed period
- New organisation charts for the OSI with many job descriptions finalised, including educational, skills and abilities requirements
- Initial review of private pension system in Jamaica by pension regulatory expert
- Prototype for an automated insurance industry financial analysis program
- First drafts of new Investment Guidelines for insurance companies, and a new Insurance Act
- Second draft of new Insurance Act sent out to all stakeholders for comment
- Examination manual and procedures.

In December 1998, working with analysts from the OSI, the project team completed an examination of Island Life, using many of these newly developed benchmarks and analyses. This was the first such on-site examination to take place in Jamaica. An examination of Life of Jamaica began on June 28, 1999. The IADB project is scheduled for completion in the year 2000.