

This exposure draft presented by Labuan FSA to provide an overview of the proposed requirements on contract certainty principles for general reinsurance arrangements undertaken by Labuan reinsurers or via Labuan reinsurance brokers. The exposure draft intends to ensure adequacy of reinsurance contract as well as minimise contractual disputes within the industry.

Labuan FSA welcomes and values feedback on the requirements of the exposure draft. The comments or inputs may encompass suggestions, recommendations and alternatives, which should be supported with clear rationale, practicality and relevance for Labuan FSA's consideration.

Feedback shall be submitted electronically to Labuan FSA using the response template by 2 October 2023 to the following officers:

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## **GUIDELINES ON CONTRACT CERTAINTY PRINCIPLES OF GENERAL REINSURANCE ARRANGEMENTS**

### **1.0 Introduction**

- 1.1 There has been increasing awareness and recognition by the international insurance markets around the world on the importance of having certainty in contract arrangements. As a result, many jurisdictions have embarked on the initiative to develop contract certainty expectation in the forms of code of practice and market guidance to enhance transparency whilst preserving the diversity and competitive position of their markets.
- 1.2 Against this backdrop, it is vital for Labuan reinsurance industry to embrace contract certainty to reap its associated benefits. This would also enhance the stature of Labuan International Business and Financial Centre (Labuan IBFC) as a modern and conducive marketplace for international reinsurance business dealings.
- 1.3 Contract certainty is important to ensure parties to the reinsurance contract such as cedants, insurance intermediaries and reinsurers understand the terms and conditions of the reinsurance coverage. It also warrants for prompt delivery of documentation evidencing coverage for the cedants.
- 1.4 The benefits of adopting contract certainty are enormous, particularly for large and complex reinsurance contracts. Essentially, it is intended to minimise reinsurance settlement and recoveries disputes which in turn reduce the legal, financial, reputational and operational risks. Although disputes may still arise with contract certainty, this would be confined to a known and agreed reinsurance document between parties to the contract.

## **2.0 Regulatory Expectations**

- 2.1 The *Guidelines on Contract Certainty Principles of General Reinsurance Arrangements* (the Guidelines) is a continuation effort to build on the regulatory expectation in relation to reinsurance contracts as specified under paragraph 9.0 of the *Guidelines on General Reinsurance Arrangements and Sound Practices* as well as paragraphs 12.0 and 14.0 of the *Guidelines on the Conduct and Roles of Labuan Insurance and Takaful Brokers*.
- 2.2 As the contract certainty initiative observed in other international markets is mostly market-driven, Labuan FSA aspires for the Labuan insurance market association<sup>1</sup> to play an active role in inculcating contract certainty within its insurance communities. In line with the expectations of the Guidelines, Labuan insurance industry may emulate the practice of other international markets in achieving contract certainty taking into account the dynamic and international nature of Labuan insurance business.
- 2.3 The Labuan insurance industry is expected to be further guided by issuance of practice notes or checklist by its association in order to ensure greater understanding on how contract certainty can be effected and achieved.

## **3.0 Applicability**

- 3.1 The Guidelines is applicable to general reinsurance (including retakaful) contracts:
- (i) entered into by a Labuan (re)insurer licensed under Part VII of the Labuan Financial Services and Securities Act 2010 (LFSSA) or a Labuan (re)takaful operator licensed under Part VII of the Labuan Islamic Financial Services and Securities Act 2010 (LIFSSA); or
  - (ii) entered into by a Labuan captive insurance business and Labuan captive takaful business licensed under Part VII of the LFSSA and Part VII of the LIFSSA, respectively; or

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<sup>1</sup> This refers to the Labuan International Insurance Association (LIIA).

- (iii) arranged through a Labuan insurance broker or a Labuan takaful broker licensed under Part VII of the LFSSA and Part VII of the LIFSSA, respectively.

#### **Question 1:**

Labuan FSA would like to seek feedback from Labuan captive insurers whether captives should be scoped in under this Guidelines? Please provide justification to support your recommendation.

### **4.0 Legal Provision**

- 4.1 The Guidelines is issued pursuant to Section 4A of the Labuan Financial Services Authority Act 1996 (LFSAA) for the purpose of clarifying the regulatory expectations on the general reinsurance arrangements to achieve contract certainty.
- 4.2 Any person who fails to comply with the Guidelines may be subject to an administrative penalty and/or other enforcement actions under Section 36B and Section 36G of the LFSAA.

#### **Question 2:**

What is your view if the contract certainty regulatory expectation is issued in any of the following form?

- (i) Guidelines which is enforceable by law as specified under paragraphs 4.1 and 4.2 above; or
- (ii) Best practices where observance to the requirements are highly encouraged and can be achieved through market consensus

Please provide your justification for the preferred option.

### **5.0 Effective Date**

- 5.1 The Guidelines shall come into effect on **DD MM 2025** and would remain effective and applicable unless amended or revoked.

## 6.0 Definitions

<b>Contract Certainty</b>	Contract certainty is achieved by the complete and final agreement of all terms between the cedant and reinsurer by the time that they enter into the contract, with contract documentation provided promptly thereafter. <sup>2</sup>
<b>Terms</b>	Refer to the contractual provisions of the contract. The agreed terms may be included by reference to either contract specific or standard/model materials.
<b>Contract Documentation</b>	Contract documentation contains all the agreed terms of the contract and details of the reinsurers' participations. Examples of contract documentation include reinsurance policy, certificate of reinsurance, signed contract wording or a complete slip.
<b>Reinsurance Arrangement</b>	Reinsurance arrangement covers reinsurance, retakaful and retrocession arrangement.

## 7.0 Reinsurance Placement

**Principle 1: The reinsurance terms is clearly specified to avoid uncertainty and agreed at the time of binding.**

- 7.1 The reinsurer and broker concerned must ensure that all terms are explicit and do not bring about any ambiguity by the time the offer is made to enter into the contract or the offer is accepted. All terms would need to be clearly specified, including any conditions or subjectivities.

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<sup>2</sup> The definition of contract certainty is in line with the concept adopted by the UK's Contract Certainty Code of Practice issued in September 2018.

- 7.2 The reinsurer and broker concerned must strive to ensure that the contract documentation, including any amendments thereto, is signed by the cedant and the reinsurer where appropriate.

**Question 3:**

Have you faced any difficulties in getting the contract documentation to be signed by all parties to the contract? If yes, can you describe such instances and whether this impedes the finalisation of the reinsurance arrangement?

- 7.3 It must be recognised that a duly executed contract documentation is the final and permanent record of the agreement reached by the client. This would serve as the basis for assessing the extent of reinsurance recoverable.
- 7.4 Where a contract documentation can only be duly executed by all parties after the effective date, the reinsurance coverage during this interim period is usually set out in less formal documents (e.g., slip, cover notes, letter of proposal, binding letter of intent, hereinafter referred to as the “summary document”). The contractually binding summary documents would, at a minimum, set out:
- (i) The premium/consideration;
  - (ii) The risk(s) reinsured;
  - (iii) The period of cover;
  - (iv) Any exclusions to terms of coverage;
  - (v) Any standard clauses that are to be relied upon or incorporated by reference into the contract documentation; and
- Any material issues that are most likely to arise and need to be addressed, including all variable or unique agreement terms.

**Principle 2: The contract documentation is provided promptly to all parties and any changes must be made by documented mutual agreement.**

- 7.5 Contract documentation is required to be provided to all parties promptly i.e. the earlier between:
- (i) the timeline as specified in any relevant terms of business agreement with clients; or
  - (ii) within 30 calendar days measured from the reference date.

- 7.6 The reference date provided under paragraph 7.3 (ii) refers to the later of:
- (i) The inception date of the contract; or
  - (ii) The date on which the parties enter into the contract. Where there is more than one participating reinsurer, the date on which the final reinsurer enters into the contract.

**Question 4:**

Do you think the suggested timeline for provision of contract documentation is reasonable? Kindly provide the rationale and alternative suggestions, if any.

- 7.7 Where a broker is involved in the preparation or delivery of the contract documentation, the reinsurer is required to provide the broker with sufficient time for any relevant checking and onward provision of the documentation within the period defined as promptly.
- 7.8 Any changes to the contract need to be certain and made by documented mutual agreement which clearly identifies the effective date of change. Documentation in respect of the change is required to be provided to the cedant promptly thereafter.

## **8.0 Placement with Multiple Reinsurers**

**Principle 3: The contract formed needs to be certain to reflect each reinsurer's final participation and avoid misunderstandings.**

- 8.1 The reinsurers and brokers concerned must avoid the practice of post-inception over-placing as such practice could compromise contract certainty principles.
- 8.2 The contract documentation must include an agreed basis on which each reinsurer's final participation will be determined. This includes the method of calculating reinsurer participations (signed lines).
- 8.3 Any contract would need to be carefully worded to ensure no subsequent misunderstandings and arguments alleging misrepresentation at a later date. The cedant must also be informed in writing about the terms agreed with each set of reinsurers by their brokers.

**Principle 4: The final participation is provided to each reinsurer promptly.**

- 8.4 The final participation must be provided to each reinsurer promptly as below:
- (i) Each reinsurer's participation on the contract will be made available by inception or upon completion of the risk placement if this occurs post-inception;
  - (ii) Where the reinsurer needs the reinsurer participations to prepare the contract documentation, then reinsurer participations must be provided by the broker in sufficient time to allow for this;
  - (iii) Where the contract documentation is to be prepared by the broker, then the reinsurer participations would need to be provided in sufficient time to allow for reinsurer authorisation of the contract documentation;
  - (iv) Each reinsurer's participation on the contract will be provided within 30 calendar days of either inception or completion of placement, whichever is the later.

**9.0 Performance Expectation**

**Principle 5: Reinsurers and brokers are expected to demonstrate their achievement of contract certainty and resolve any exceptions without undue delay.**

- 9.1 The reinsurers and brokers concerned must be able to demonstrate the following:
- (i) Agreement of all terms was achieved by the time of entering the contract or inception date (whichever is later);
  - (ii) Contract documentation was provided promptly; and
  - (iii) The manner exceptions were identified and resolved and the actions taken to reduce occurrence.
- 9.2 The methodology for demonstrating performance would need to be consistent. Examples of how contract certainty can be demonstrated include:
- (i) Verification against a checklist;
  - (ii) Sample or file audits; and/or
  - (iii) Internal policies and controls.



- 9.3 If all terms have not been agreed by the time of entering into the contract or if accurate contract documentation has not been provided promptly, then every effort would need to be made to do so as soon as practicable thereafter.
- 9.4 If significant delay beyond the required timescales is expected, then the reinsurer or broker concerned must inform the cedant.
- 9.5 The reinsurers and brokers concerned are required to resolve any legacy backlog of contract documentation.

**Labuan Financial Services Authority**  
**XX XX 2023**

**Question 5:**

Labuan FSA seeks comments on the ED's overall requirement, including the following areas:

- i. Suggested best practices (including examples) for the proposed principles in the ED;
- ii. Issues related to uncertainties of reinsurance contracts that you have entered into in Labuan IBFC including the outcome and action taken to address the issues in detail;
- iii. Challenges in implementing the ED's requirements; and
- iv. Any suggestions for enhancement to the ED.